The great reallocation

Global private equity investors are pivoting away from China towards emerging markets like Indonesia, Vietnam, and India, driven by concerns over China's growth and geopolitical risks. These alternative markets have shown significant momentum, with India's PE investments reaching $15 billion in 2024 and Vietnam achieving over 7 percent of GDP growth. However, lawyers say success in these markets requires navigating complex local regulations and building strong partnerships with local entities. **By Nimitt Dixit**

- **Regulatory reforms across emerging Asian markets are creating more investor-friendly business environments.**
- **Private equity firms must navigate local partnerships and complex regulations for successful investments.**
- **ESG compliance and infrastructure development are becoming crucial factors in Asian investment decisions.**

The global headwinds of change are sweeping through Asia's private equity landscape as fund managers and LPs grow increasingly sceptical of China's muted growth and look beyond their most profitable Asian market to find a new home for their capital.

This pivot, while not a complete exodus from the world's second-largest economy, marks a strategic reorientation towards markets in South and Southeast Asia, with Indonesia, Vietnam and India emerging as clear favourites, while Japan experiences a dealmaking renaissance driven by corporate governance reforms, a weakening yen, and a favourable monetary environment.

Recent data paints a compelling picture of this transformation. The share of venture capital deals in China involving non-domestic investors hit its lowest level since 2015, dropping to 5.6 percent of total deals in 2024, according to Finex, a Hong Kong-headquartered private equity platform. A Probitas Partners private equity survey for 2024 found that just 3 percent of institutional investors viewed China as the "most attractive" market in Asia, down from 58 percent in 2021.

"This trend indicates a strategic reallocation of capital towards markets with better growth prospects and lower geopolitical risks," explains Gerrit Jan Kleute, principal at Baker McKenzie Wong & Leow in Singapore.

"While many funds remain invested in China, their enthusiasm for deploying fresh capital is tempered," says Harshita Srivastava, co-head of Indian law firm Nishith Desai Associates' M&A and private equity practice.

Risk mitigation and strategic adaptation

As we move through 2025, PE funds are adopting sophisticated risk-mitigation strategies in their China portfolios.

There's an increased focus on assets benefiting from domestic consumption in China, particularly consumables and healthcare-related products. "Consumption-related businesses, assets with less exposure to tariffs and export control regimes, and with the potential to expand within the Chinese market, were more attractive to investors in the current climate," explains Oliver Nip, a Hong Kong-based partner at U.S. law firm Ropes & Gray.

Firms are also identifying offshore businesses that could benefit from China's potential economic rebound while maintaining geographic diversification. "Such 'China ex-China' strategies also include targets that can diversify an investor's geographic footprint (through organic growth or bolt-on acquisitions), with expanding into Southeast Asia being a common theme," Nip adds.

China still offers attractive investment opportunities in the domestic consumption markets, owing to muted valuations and less international risk, but funds are reluctant to pull the trigger, choosing rather to wait and watch as uncertainties associated with the Trump presidency play out.

In the meantime, dry powder piles up, and there is an urgent need to find deployment vehicles in other parts of Asia. "Countries like India, Vietnam, Indonesia, and Malaysia are increasingly viewed as attractive alternatives, offering strong growth potential, favourable demographics, and a relatively stable regulatory environment," Srivastava says.

This movement is particularly evident in sectors less exposed to geopolitical risks, such as domestic consumption, healthcare, and technology. Infrastructure and social infrastructure sectors are also expected to grow, with particular interest in data centres and energy transition assets.

But the reallocation of PE investments across Asia represents more than just a reaction to China's slowdown – it's a strategic recalibration that recognises the diverse opportunities across the region. While China remains an important market, fund managers are increasingly adopting a more balanced approach to portfolio allocation.

However, regulatory and financial uncertainty - typical in emerging markets - particularly related to investment entry and exit, means investors are expressing caution before plunging into these high-growth markets, which has resulted in a significant cooldown in dealmaking across the Asia-Pacific region.

Legal experts say that success in this evolving landscape requires a nuanced understanding of local markets, regulatory frameworks, and risk factors. PE firms that can effectively navigate these complexities while building strong local partnerships are likely to find significant opportunities in Asia's emerging markets.

Indonesia: The rising star

Indonesia's emergence as a prime investment destination is no coincidence. The country's private equity market alone is projected to reach a deal value of $6.68 billion by 2025. Strong economic fundamentals, along with a young and tech-savvy population, have created ideal conditions for PE investors. Specifically, the e-commerce market is expected to reach $59.34 billion by 2025, with an annual growth rate of 7.52 percent.

"Additionally, the healthcare and renewable energy sectors are gaining traction, driven by rising demand for quality healthcare services and the government's commitment to sustainability," Kleute says.

"Indonesia's middle class is demanding higher-quality products and services, which presents opportunities for PE firms to invest in sectors such as healthcare and consumer goods. These factors indicate a positive outlook for PE investment in Indonesia in 2025," adds Daniel Pardede, senior partner at HHP Law Firm, Baker McKenzie's partner firm in Indonesia.

However, the archipelago's strengthening economic ties with China may expose it to Trump-led financial embargos. China and Indonesia have signed business deals totalling more than $10 billion and agreed to strengthen cooperation in lithium batteries and other key sectors, following President Prabowo Subianto's meeting with Xi Jinping in Beijing during his first foreign trip since inauguration.

Prabowo's "friends-with-all" strategy may face challenges in the U.S. if the Trump administration pressures Indonesia to take a clearer position on Beijing's regional ambitions. However,

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— Daniel Pardede, HHP Law Firm

experts believe increased sanctions on China could make Indonesia more attractive as a manufacturing base – a position the Indonesian administration has been pitching aggressively to international decision-makers.

Indonesia, which has a practical monopoly on nickel, aims to improve its position in the electric-vehicle value chain, transitioning from nickel exporter to global EV manufacturing hub by offering attractive tax incentives to global car manufacturers. Three carmakers—BYD, GAC Aion, and Citroen—have committed to building factories in Indonesia in 2025. They will benefit from import tax exemptions for machinery and equipment, and a reduced luxury sales tax rate of 15 percent. These incentives are designed to lower the cost of manufacturing and encourage more foreign investment in the EV sector.

What makes Indonesia particularly attractive is its evolving regulatory landscape. The country has made significant strides in improving its investment climate through the Investment Law and the Omnibus Law, which have opened most business sectors to 100 percent foreign investment. The implementation of the Online Single Submission (OSS) system has further streamlined the licensing process.

However, challenges remain, particularly in navigating foreign ownership restrictions in certain sectors. To address these hurdles, PE funds are adopting innovative approaches. "Firms are increasingly structuring their investments through joint ventures, convertible loan instruments, or minority investments in public company structures," explains Pardede.

Nevertheless, Indonesia's strong economic fundamentals and proactive government policies are likely to mitigate these challenges and enhance its competitive position. "Compared to other Southeast Asian destinations, Indonesia's large consumer market, strategic location, and diverse economic sectors make it a compelling choice for PE investments in 2025 and beyond," Pardede adds.

India's transformative moment

India's position in the Asian PE landscape has strengthened considerably, driven by initiatives like Make In India and Production Linked Incentive schemes. The country's expanding market opportunities, cost efficiencies, and competitive advantages have caught the attention of global investors.

The country's ascent in the private equity landscape is marked by impressive numbers and transformative developments that are reshaping its investment ecosystem. The country achieved a remarkable milestone, with gross foreign direct investment (FDI) reaching $1 trillion since April 2000. Private equity investments in India surged to $15 billion in 2024, marking a 46.2 percent increase from the previous year, as shown by data analysed by LSEG Deals Intelligence. This growth was driven by sectors such as healthcare and pharmaceuticals, consumer-related industries, and technology.

"India is increasingly establishing itself as a standout destination in Asia's PE landscape," observes Srivastava. "We are seeing global funds increasingly adopting India-specific strategies to capitalise on its long-term growth story."

India remains one of the top markets in the Asia Pacific for financial sponsor activity, accounting for at least 28 percent of the region's total equity investments during this period, up from a 15 percent market share the previous year. However, fundraising showed some weakness, with a 29 percent decrease year-over-year to $4.3 billion, though the total PE funds raised over the past three years remained robust at approximately $23 billion.

The market was dominated by several significant transactions that shaped the investment landscape. Data Infrastructure Trust led the pack with a substantial $2.17 billion investment through a single transaction spanning three firms. Kiranakart Technologies followed with multiple deals totalling $1.36 billion, while Hyundai Motor India secured $989 million in the transportation sector. Other notable investments included Manash Lifestyle at $298.3 million and Fourth Partner Energy at $274 million, demonstrating the diverse nature of investment interests across sectors.

The Internet-specific sector led investments, attracting $4.49 billion across 368 deals, marking a 15.8 percent year-over-year increase. The communications sector witnessed extraordinary growth of 5,963.4 percent, securing $2.22 billion across seven deals.

Healthcare demonstrated significant momentum, with medical/health investments increasing by 66.4 percent to reach $817 million across 58 deals. The biotechnology industry showed remarkable growth with a 503.7 percent increase, while the construction sector posted a 14,219.2 percent increase.

However, regulatory challenges persist, notably Press Note 3, which imposes restrictions on investments from countries sharing land borders with India.

"From a foreign exchange perspective, besides sectoral caps and sectoral specific conditions in some cases, I think the biggest hurdle in recent times has been the Press Note 3, which imposes restrictions on investments from countries sharing land borders with India,

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impacting funds with exposure to these jurisdictions," Srivastava explains.

"To address these, firms are leveraging local expertise, adopting tailored deal structures, and proactively engaging with regulators to ensure compliance and mitigate risks," she adds.

Slow litigation and arbitration outcomes and uncertainty over enforcement of exit mechanisms remain concerns. The National Company Law Tribunal allots only one out of six working days to M&A approvals, significantly slowing dealmaking. While regulatory reforms, including increased bench strength address these bottlenecks, investors remain cautious about entry and exit timelines.

The country's new merger control guidelines, upcoming data regulations and heightened scrutiny over the financial technology and banking space threaten to elongate timelines for investment and increase compliance costs, but an increased emphasis on transparency and global ESG alignment give comfort to global capital looking to make India its new home.

Looking ahead to 2025, India's PE market is expected to gain further momentum. Sectors such as AI, blockchain, cryptocurrency, pharma and healthcare, renewable energy, and EV infrastructure are projected to attract substantial investments.

"Investors should watch out for easing of FDI norms, including clarity on PN3, 100 percent FDI under automatic route in insurance," Srivastava says.

Vietnam: The next frontier

Vietnam's emergence as an investment destination presents a nuanced picture. The country surpassed all socioeconomic targets set by the National Assembly for 2024, with GDP growth exceeding 7 percent. HSBC economists predict that Vietnam will achieve the highest GDP growth among the six largest Southeast Asian economies in 2025.

The government's focus on digitalisation and energy transition is attracting global attention from conglomerates and fund managers alike, priming the country for a busy year of private equity investments and dealmaking.

"Compared to other Southeast Asian markets, Vietnamese equities are considered cheaper than those in neighbouring countries, offering investors an attractive entry point," explains Nguyen Van Hai, a partner at Vietnamese law firm YKVN.

"Remarkable deals have been observed in education, healthcare, and consumer goods, as Vietnamese consumers increasingly spend more on these services and products. Additionally, the 'China Plus One' strategy has made industrial real estate an attractive sector for capital deployment," Hai adds.

But some experts say this rapid growth is yet to transform into promised results. "While global funds have increased their focus on Vietnam, actual investments remain relatively limited," says Ngoc Anh Bui, the managing partner of Vietnamese law firm VILAF's Hanoi office.

Key reasons for this slow pace are the country's well-established capital controls and restrictions on foreign ownerships.

The capital control or foreign exchange risk has still been the issue affecting the investment decisions as the investment is required in Vietnamese dong, both at the beginning and exit, Bui explains, adding that this should be categorised as a hurdle rather than a risk as it has always been easy to exchange dong with the U.S. dollar in the country.

In terms of market access, Vietnam still enforces foreign ownership limits in several business segments, such as telecommunications and logistics, which can hinder control acquisitions by foreign investors, Hai notes.

Another key challenge is the lengthy approval process for investments, which is typical of an emerging market. "Obtaining inbound investment approvals remains time-consuming, often taking up to a month for unregulated business sectors," notes Hai.

While problems persist, the Vietnamese authorities have demonstrated strong commitment to reform, enacting new laws to remove legal obstacles for investments. The recent passage of laws amending multiple existing regulations, along with new Land Law and Electricity Law, signals a positive shift in the investment climate. Proposals for projects like the North-South high-speed railway and nuclear power plants further underscore the government's support.

PE investors should also anticipate enhanced regulations related to data localisation, cybersecurity, and the cross-border transfer of data in 2025. "These regulations may impose stricter requirements on data storage, processing, and protection, potentially impacting the operations of portfolio companies, especially in technology, e-commerce, and fintech sectors," Hai warns.

The government is also likely to prioritise further infrastructure development and attract high-quality investments, including those in technology sectors such as data centres and ESG-compliant industries.

"To succeed in Vietnam's evolving ESG landscape, PE investors must proactively integrate ESG factors into their investment strategies and portfolio company engagement," Hai notes.