Vietnam at the Crossroads

Manufacturing FDI, Transshipment Enforcement, and the Tariff Tightrope

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Abstract

Vietnam enters 2026 as the most dynamic manufacturing story in Southeast Asia, with real GDP growth of 6.0 to 6.5% underpinned by resilient foreign direct investment, an electronics export complex that keeps deepening, and a diversification tailwind from the EU Vietnam Free Trade Agreement. Yet the same feature that made Vietnam indispensable to global supply chains, its role as the primary relocation node in the China plus one shift, now sits at the center of its largest risk. Washington has moved from tariff threats to active rules of origin enforcement, and a 40% transshipment penalty on goods deemed to be rerouted Chinese content hangs over the export model. This paper argues that Vietnam is attractively positioned but requires active monitoring rather than passive conviction. We hold Vietnam at Market weight, above regional laggards yet below our highest structural convictions in India and Indonesia, and we specify the enforcement and currency catalysts that would move us either way.

1. The Setup: Southeast Asia's Growth Engine Meets a Trade Policy Vise

Vietnam is the clearest embodiment of a decade long structural thesis: as multinationals de risked away from concentrated Chinese production, Vietnam absorbed the largest share of relocated capacity in labor intensive electronics, footwear, furniture, and increasingly mid tier semiconductor assembly and test. That thesis delivered. Real GDP expanded above 7% in 2024 and held near the top of the ASEAN range through 2025, and we forecast 6.0 to 6.5% for 2026, comfortably above the roughly 4.4% Asia Pacific aggregate in the Darmine house baseline. The composition matters as much as the headline. Growth is externally geared, investment led, and concentrated in a manufacturing base that has moved up the complexity curve faster than most peers at Vietnam's income level.

The problem is that this success now collides with a US trade policy regime that has shifted from broad tariff walls to surgical enforcement. The China plus one playbook worked precisely because Vietnam offered lower labor costs, proximity to Chinese component suppliers, and preferential or neutral access to Western markets. Washington has concluded that a meaningful share of the resulting trade is not genuine value added in Vietnam but Chinese content lightly finished and relabeled. The policy response, rules of origin scrutiny backed by a punitive transshipment tariff, targets exactly the seam that Vietnam's model was built on. Vietnam therefore sits at a genuine crossroads, not a rhetorical one.

> **Our view:** Vietnam is the highest quality growth story in ASEAN outside of the giants, but its beta to a single external variable, US enforcement intensity, is higher than any other economy we cover. We treat it as a Market weight with asymmetric catalysts rather than a passive Overweight.

2. The Manufacturing Base: What Vietnam Actually Makes and Why It Keeps Winning FDI

Vietnam's export engine is dominated by electronics. Smartphones, components, computers, and related equipment now account for roughly a third of total merchandise exports, anchored by a large Samsung production footprint that alone represents a meaningful slice of national output, alongside a growing roster of Apple contract manufacturers, LG, Foxconn, Luxshare, and a widening base of second tier suppliers. Around this core sits a mature ecosystem in textiles and footwear, wood products and furniture, and machinery. This is not a commodity export story vulnerable to a single price cycle; it is a diversified light to mid manufacturing complex with rising domestic linkages.

Foreign direct investment remains the fuel. Registered FDI has held near record levels, and, more importantly for near term activity, disbursed FDI has stayed resilient even as global merchandise trade volume growth decelerates to only around 0.5% in 2026 in the WTO framing we use in the house baseline. Investors continue to choose Vietnam for a combination that is hard to replicate at scale in the region: a young and disciplined workforce, competitive unit labor costs, deepening supplier density, improving logistics, and a government that has been aggressive on industrial parks, power capacity, and free trade agreements. The result is that even in a soft global trade year, Vietnam's capital formation continues to run ahead of the regional pack.

2.1 Moving Up the Curve, But Still Import Dependent

The critical nuance is that Vietnamese manufacturing remains heavily reliant on imported inputs, a large share of them Chinese. Components, intermediate goods, fabric, and machinery flow in from China, are assembled or finished in Vietnam, and ship out to the United States and Europe. In a normal trade regime this is simply an efficient regional value chain. Under an aggressive rules of origin regime it is the precise pattern that triggers transshipment scrutiny. Vietnam's dependence on Chinese intermediates is both the source of its cost competitiveness and the origin of its enforcement vulnerability. The country's medium term challenge is to raise domestic value added fast enough to stay clearly on the right side of origin rules.

> **Our view:** The manufacturing base is genuinely strong and diversifying, but the import intensity of exports is the fault line. We want to see rising local content ratios, not just rising export headlines, before we would upgrade Vietnam toward Overweight.

3. The Central Risk: US Transshipment Enforcement and Rules of Origin

The defining feature of Vietnam's 2026 is the bilateral trade framework with the United States. The operative structure pairs a baseline tariff on genuinely Vietnamese goods with a substantially higher penalty rate, in the region of 40%, on goods judged to be transshipped, meaning Chinese content routed through Vietnam with insufficient local transformation. The baseline rate itself, around the 20% area, is manageable and lower than the punitive effective rates applied to China at 47.5% and to India at 36% in our baseline. The differential between the baseline and the transshipment penalty is the entire game. It converts a broad tariff question into a granular, product by product, factory by factory origin question.

This is why enforcement intensity, not the headline rate, is the variable we monitor. If US Customs and the relevant agencies apply origin rules loosely, most of Vietnam's electronics complex clears at the baseline and the growth thesis is intact. If enforcement tightens, with stricter regional value content thresholds, more aggressive audits, and expanded documentation demands, then a swath of assembly heavy, import intensive exports could be reclassified into the penalty band. The economic difference between those two worlds is large, and the outcome depends on administrative and political choices in Washington that are difficult to forecast with precision.

3.1 Scenario Framing

We frame the enforcement question as three states rather than a point estimate, because the distribution is what matters for positioning. In the benign state, enforcement stays procedural and predictable, local content rules are met by most large exporters, and Vietnam compounds its share gains. In the base state, enforcement is real but targeted, a minority of the most obviously rerouted product lines gets penalized, and exporters respond by deepening local sourcing and tightening documentation, shaving perhaps a few tenths off growth. In the adverse state, enforcement broadens, ambiguity itself deters investment decisions, and both the FDI pipeline and export momentum slow materially.

Enforcement scenario	Approx. probability	Effective US access	2026 GDP impact vs base	FDI signal
Benign (procedural)	25%	Baseline ~20% on most lines	+0.3 to +0.5 pt	Pipeline accelerates
Base (targeted)	50%	Baseline plus penalties on select lines	Neutral, our 6.0 to 6.5% call	Pipeline resilient, cautious
Adverse (broad)	25%	40% penalty on wide product set	-1.0 to -1.5 pt	Pipeline pauses, some deferral

Darmine estimates. Baseline tariff and 40% transshipment penalty are illustrative of the operative US Vietnam framework; probabilities reflect our subjective distribution as of May 2026.

> **Our view:** We assign roughly even tail risks around a targeted base case. Because the adverse tail is genuinely disruptive rather than merely a growth trim, Vietnam does not earn an Overweight at current visibility. This is the single most important judgment in the paper.

4. The Diversification Hedge: The EU Vietnam FTA and Market Rebalancing

Vietnam's most important structural hedge against US concentration is Europe. The EU Vietnam Free Trade Agreement continues to phase out tariffs across the vast majority of tariff lines, and it gives Vietnamese exporters preferential access to a market of comparable scale to the United States. As US policy risk rises, the relative attractiveness of the European channel increases, and we expect exporters, particularly in footwear, textiles, agricultural products, and consumer electronics, to lean into it. Diversifying the destination mix does not neutralize US enforcement risk, but it lowers the economy's single market dependence and gives firms a credible alternative when routing decisions are made.

Crucially, the EU agreement carries its own rules of origin, and meeting them pushes Vietnamese producers in exactly the direction that also de risks the US relationship: higher local and regional value content, better documentation, and less reliance on lightly transformed Chinese inputs. The discipline required to maximize EU preferential access is complementary to the discipline required to stay on the safe side of US transshipment rules.

This is the constructive interpretation of the enforcement squeeze: it accelerates an upgrading that Vietnam needed to undertake regardless.

> **Our view:** The EU FTA is underappreciated as a shock absorber. It both diversifies demand and nudges the supply base toward the higher local content model that ultimately protects US access. We view it as a genuine, if gradual, structural positive.

5. The Dong and Macro Stability: Managing the External Account Under Pressure

Currency is where trade risk becomes financial risk. The Vietnamese dong has faced persistent depreciation pressure against a firm US dollar, and the State Bank of Vietnam has managed a gradual, controlled weakening rather than defending a hard line, allowing the exchange rate to drift toward the weaker end of its reference band while intervening to prevent disorderly moves. A softer dong supports export competitiveness at the margin, which is helpful when tariffs raise landed costs, but it also imports inflation, pressures dollar liabilities, and constrains how much monetary easing the central bank can deliver to support domestic demand.

The policy tension is real. Vietnam would like lower rates to sustain credit growth and property market stabilization, but aggressive easing risks accelerating dong depreciation and, more sensitively, inviting exactly the currency manipulation scrutiny that dovetails with the transshipment narrative in Washington. The State Bank is therefore threading a narrow path: enough flexibility to keep exporters competitive and credit flowing, but enough restraint to avoid a disorderly slide or a political flashpoint on the currency. Foreign reserves provide a buffer, but not an unlimited one, and reserve adequacy is a metric we watch closely as an early indicator of stress.

5.1 Inflation and Domestic Demand

Beneath the external story, domestic demand is a supporting actor with real momentum. A young population, a rising middle class, urbanization, and a recovering tourism sector underpin consumption, while public investment in infrastructure, power, and transport provides a second engine less exposed to trade policy. Inflation has been contained enough to give the central bank some room, though a weaker dong keeps the risk skewed to the upside. The domestic pillar is what allows us to argue that even in a moderately adverse enforcement scenario, Vietnam does not collapse; it decelerates from an exceptional pace to a merely good one.

> **Our view:** Watch the dong and reserves as the fast moving stress gauge. A controlled drift is fine and even helpful; a step change in depreciation or a visible reserve drawdown would signal that trade pressure is metastasizing into financial pressure, and would push us toward Underweight.

6. Vietnam in the Regional Context: Relative Positioning Across ASEAN and Asia

Vietnam's attractiveness is best judged against peers rather than in isolation. On growth, it sits at or near the top of the region, with our 6.0 to 6.5% call rivaled only by India's roughly 6.5% among the major economies we cover, and well ahead of Thailand's 1.8 to 2.5%, Malaysia, and even Indonesia's roughly 5.0%. On structural conviction, however, the ranking inverts. India and Indonesia earn our clearest Overweights because their growth is anchored in vast domestic markets that are relatively insulated from US enforcement mechanics, while Vietnam's export gearing makes it more exposed to a single external policy switch.

The comparison with China is instructive. China faces a 47.5% effective US tariff, fading exports, persistent deflation, and a property overhang, and we are Underweight Chinese domestic demand. Vietnam is in many respects the beneficiary of China's predicament, capturing relocated capacity, yet it remains umbilically linked to Chinese inputs. Vietnam's fortunes are therefore a leveraged, and partially hedged, play on the same US China rivalry that weighs on China directly. Against Singapore, our Overweight quality defense pick, Vietnam offers far more growth but far less institutional depth and policy predictability. The regional table below situates Vietnam within our house framework.

Economy	2026 GDP growth	Effective US tariff regime	Primary driver	Darmine stance
Vietnam	6.0 to 6.5%	~20% base, 40% transship penalty	Manufacturing FDI, electronics	Market weight
India	~6.5%	36% effective	Domestic demand	Overweight
Indonesia	~5.0%	Moderate	Nickel, EV batteries	Overweight
China	~4.4 to 4.5%	47.5% effective	Fading exports, deflation	Underweight (domestic)
Singapore	2.0 to 4.0%	Low	Quality, S NEER appreciation	Overweight
Thailand	1.8 to 2.5%	Moderate	Autos, tourism (weak)	Underweight

Darmine house baseline, May 2026. Growth figures are Darmine central estimates consistent with IMF and World Bank regional outlooks.

> **Our view:** Ranked purely on growth, Vietnam is second only to India. Ranked on risk adjusted structural conviction, it slots behind India, Indonesia, and Singapore. That gap between raw growth and conviction is exactly what Market weight is meant to express.

7. Investment Implications and What Would Change Our Mind

For investors, Vietnam offers a high growth, high policy beta profile that rewards selectivity over blanket exposure. Within the equity market we prefer exporters with demonstrably high local value content and diversified end markets, domestic consumption names insulated from trade mechanics, banks levered to credit growth but with manageable dollar funding, and industrial and logistics real estate that benefits from continued FDI regardless of which specific product lines get scrutinized. We are more cautious on pure assembly plays whose margins depend on lightly transformed imported content, since these carry the most direct transshipment exposure.

The macro case for Vietnam is that it is structurally cheap relative to its growth, under owned by many global allocators, and positioned at the center of the single most important supply chain realignment of the decade. The macro case against it is concentration: too much depends on the US enforcement dial and the dong. Our resolution is to hold Market weight and to be explicit about the observable signals that would move us. This is a name to monitor actively, adding on evidence that enforcement is settling into a predictable, procedural regime and trimming on evidence that the adverse tail is materializing.

- Upgrade toward Overweight if: US enforcement stabilizes into a clear, procedural, product level regime; local content ratios in electronics rise measurably; the FDI pipeline reaccelerates; and the dong stabilizes.
- Downgrade toward Underweight if: transshipment penalties broaden to core electronics lines; the dong depreciation becomes disorderly or reserves draw down sharply; or currency manipulation scrutiny escalates into formal action.
- Prefer: high local content exporters, domestic consumption, industrial and logistics real estate, and banks with contained dollar funding.
- Avoid or underweight: thin margin assembly operations most exposed to origin reclassification.

> **Our view:** Vietnam is a monitor and add name, not a set and forget one. The right posture is Market weight now with a clearly defined path to Overweight, contingent on enforcement clarity and rising domestic value added.

Portfolio Positioning Summary

Overweight: India and Indonesia remain our highest structural convictions in Asia, anchored by large domestic markets relatively insulated from US enforcement mechanics; Singapore is our quality defense Overweight. Vietnam is not here yet, but has the clearest path to promotion of any Market weight in our coverage.

Market weight: Vietnam. Best in class ASEAN growth at 6.0 to 6.5%, driven by resilient manufacturing FDI and a deepening electronics complex, hedged by the EU Vietnam FTA, but held at Market weight because of asymmetric exposure to a single external variable: US transshipment enforcement. We add on enforcement clarity and rising local content; we hold pending both.

Underweight: China domestic demand (47.5% tariff, deflation, property overhang) and Thailand (regional laggard at 1.8 to 2.5%, high household debt, weak China tourism). Vietnam would migrate here only in the adverse enforcement scenario, on broadening penalties or disorderly dong depreciation.

Key catalysts to reassess: Reassess on: US Customs enforcement posture and any expansion of transshipment reclassification; measured local content ratios in the electronics complex; disbursed FDI trend; State Bank of Vietnam dong management and reserve adequacy; EU FTA utilization rates; and any escalation of US currency scrutiny.

Conclusion

Vietnam is genuinely attractively positioned. It runs the fastest growth in ASEAN outside the giants, it keeps winning the foreign investment that the region's slower economies covet, its electronics base is diversifying and moving up the value curve, and the EU Vietnam FTA gives it a real hedge against over dependence on the American market. In a year when global merchandise trade volume growth stalls near 0.5% and much of Asia settles for around 4.4%, Vietnam's 6.0 to 6.5% is a standout that reflects durable structural advantages rather than a cyclical bounce.

But the crossroads in our title is not rhetorical. The same import intensive, China linked value chain that makes Vietnam cheap and fast is the exact pattern that US rules of origin enforcement is built to catch, and the gap between the roughly 20% baseline tariff and the 40% transshipment penalty is wide enough that administrative choices in Washington, not fundamentals in Hanoi, will determine which Vietnam investors get. We therefore hold Vietnam at Market weight: above the regional laggards, below our clearest convictions, and with a well specified path to Overweight that runs through enforcement clarity, rising domestic value added, and a stable dong. Vietnam rewards active monitoring, not passive faith, and that is precisely how we intend to hold it.

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