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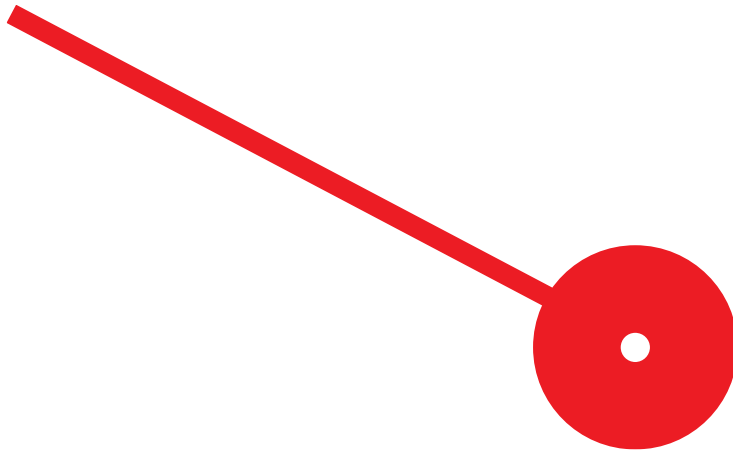
MASTER  
INTERCULTURAL STUDIES FOR BUSINESS

**Connecting China to Europe  
through Luxembourg: How does a  
small country act as a financial  
bridge for China's aspirations In  
Europe?**

**João Miguel Martins Cunha**

Final version (This version contains the jury's input and suggestions)

10/2024



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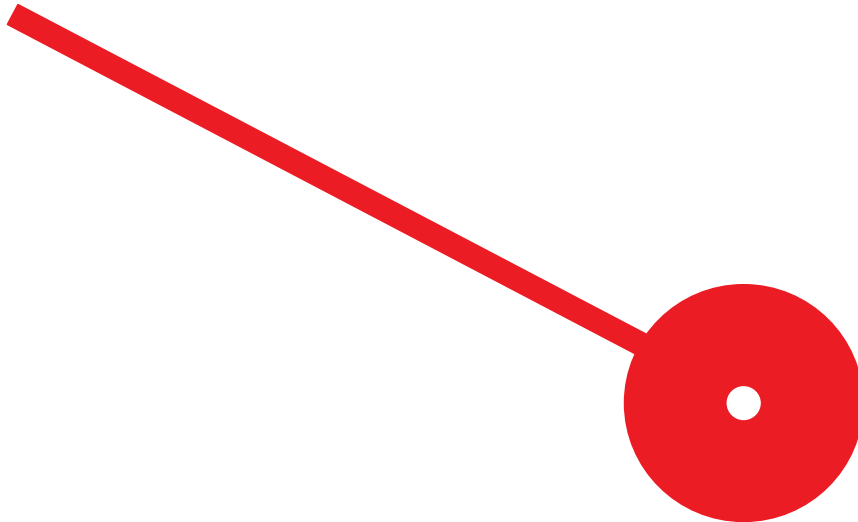
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Connecting China to Europe through  
Luxembourg: How does a small country act  
as a financial bridge for China's  
aspirations In Europe?

João Miguel Martins Cunha

Dissertation presented to Instituto de  
Contabilidade e Administração do Porto to obtain  
the Master's Degree in Intercultural Studies for  
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Master Sara Costa

João Miguel Martins Cunha. Connecting China to Europe through  
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“I want to thank me for believing in me, I want to thank me for doing all this hard work. I want to thank me for having no days off. I want to thank me for never quitting [...] I want to thank me for being me at all times.” – Snoop Dogg.

I would like to express my appreciation to my parents for their endless love and support throughout my academic journey. I will always be in owe of what you two have sacrificed to make this possible.

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To those who were with me in spirit, witnessing me shine throughout my academic experience, I am grateful for all your divine support and guidance when I felt like giving up. As the song goes, "Wish You Were Here" - your presence, even from afar, has been a guiding light.

“This is for everybody going through times  
Believe me, been there, done that  
But every day above ground is a great day, remember that”

- Pitbull

## **Resumo:**

Esta tese examina o desenvolvimento dos laços financeiros entre a China e o Luxemburgo, com este país a servir de ponto de entrada fundamental para os investimentos chineses no mercado único europeu. Luxemburgo é examinado desde antigas condições económicas para um crescimento significativo como centro financeiro, mantendo uma posição pró-europeia e um compromisso global. A investigação centra-se nas mudanças económicas, na troca comercial e no investimento direto estrangeiro da China. Além disso, a investigação descreve em pormenor os primeiros compromissos diplomáticos que conduziram às actuais alianças económicas, salientando o papel dos bancos chineses no Luxemburgo e a forma como estão a influenciar o sector financeiro na Europa. O programa QFII/RQFII e a regulação UCITS são citados como exemplos para demonstrar a disponibilidade do Luxemburgo em aceder aos mercados chineses. O tratado de dupla tributação Luxemburgo-Hong Kong e os fundos de investimentos alternativos são citados como exemplos para demonstrar a disponibilidade do Luxemburgo em reencaminhar os investimentos chineses para a Europa e para o país respetivamente.

O trabalho investiga, ainda, o impacto mais amplo das políticas financeiras do Luxemburgo e o seu alinhamento com a estratégia económica mundial da China, como a Iniciativa “Uma Rota, Uma Faixa”. A análise inclui também um estudo sobre tecnologia financeira e finanças verdes para demonstrar a capacidade do Luxemburgo para se ajustar e planear antecipadamente as suas interações económicas com a China. A tese examina as interações culturais resultantes destas ligações financeiras, tais como o afluxo de emigrantes chineses e o avanço da cultura chinesa no Luxemburgo. Estes factores culturais reforçam a compreensão e a relação bidirecional para além da simples relação financeira.

**Palavras chave:** Relações financeiras sino-luxemburguesas, Internacionalização do Renminbi, Investimentos Chineses na Europa, Iniciativa “Uma Faixa, Uma Rota”.

## **Abstract:**

This thesis examines the development of financial ties between China and Luxembourg, with Luxembourg serving as a key entry point for Chinese investment in the European single market. Luxembourg is examined from former economic conditions to significant growth as a financial center, while maintaining a pro-European stance and global commitment. The research focuses on China's economic changes, trade and foreign direct investment. In addition, the research details the early diplomatic engagements that led to the current economic alliances, highlighting the role of Chinese banks in Luxembourg and how they are influencing the financial sector in Europe. The QFII/RQFII programme and the UCITS regulation are cited as examples to demonstrate Luxembourg's willingness to access Chinese markets. The Luxembourg-Hong Kong double taxation treaty and alternative investment funds are cited as examples to demonstrate Luxembourg's willingness to redirect Chinese investments to Europe and to the country respectively.

The work also investigates the broader impact of Luxembourg's financial policies and their alignment with China's global economic strategy, such as the “One Belt, One Road” Initiative. The analysis includes a study on financial technology and green finance to demonstrate Luxembourg's ability to adjust and plan ahead for its economic interactions with China. The thesis examines the cultural interactions resulting from these financial links, such as the influx of Chinese emigrants and the advancement of Chinese culture in Luxembourg. These cultural factors enhance understanding and the two-way relationship beyond the simple financial relationship.

**Key words:** Sino-Luxembourg Financial Relations, Renminbi Internationalization, Chinese Investments in Europe, Belt and Road Initiative.

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## **List of abbreviations**

AIF - Alternative Investment Funds

AIFMD - Alternative Investment Fund Managers Directive

AIIB – Asian Infrastructure Investment Bank

ASEAN - Association of Southeast Asian Nations

BRI - Belt and Road Initiative

BLEU - Belgium-Luxembourg Economic Union

Benelux - Belgium, Netherlands, Luxembourg

CACEIS - Crédit Agricole Caisse d'Épargne Investor Services

CDIRS - Chengdu International Railway Service

CFL - Société Nationale des Chemins de Fer Luxembourgeois

CSRC - China Securities Regulatory Commission

CSSF - Commission de Surveillance du Secteur Financier

ECSC - European Coal and Steel Community

EEC - European Economic Community

ESG - Environmental, Social, and Governance

EU - European Union

EUR - Euro

FDI - Foreign Direct Investment

Fintech - Financial Technology

GDP - Gross Domestic Product

HNCA - Henan Civil Aviation Development & Investment Co.

LuxSE - Luxembourg Stock Exchange

MoU - Memorandum of Understanding

MRF - Mutual Recognition of Funds

NATO – North Atlantic Treaty Organization

QFII - Qualified Foreign Institutional Investor

R&D - Research and Development

RMB - Renminbi

RQFII - Renminbi Qualified Foreign Institutional Investor

RCEP - Regional Comprehensive Economic Partnership

RTSB - Rail Transportation Service Broker

SA - Société Anonyme

SARL - Société à Responsabilité Limitée

SICAR - Société d'Investissement en Capital à Risque

SICAV - Société d'Investissement à Capital Variable

SIF - Specialized Investment Fund

SOE - State-Owned Enterprises

UCITS - Undertakings for Collective Investment in Transferable Securities

USD - United States Dollar

VAT - Value Added Tax

# **INTRODUCTION**

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When I visited Luxembourg, I was struck by an unexpected sight at the airport: a large advertisement for the "Bank of China," prominently displayed alongside Chinese characters. As I strolled through the city center, I noticed the presence of more Chinese banks, sparking my curiosity about how such strong ties had been forged between this small European nation and one of the world's largest economies. The more I observed, the more I wondered why Luxembourg, despite its modest size, had become a hub for Chinese financial institutions. This intrigue led me to delve deeper into the factors behind China's interest in Luxembourg.

Although small, Luxembourg has become a prominent financial center globally, attracting Chinese financial institutions and granting them a gateway to the European single market. Putting aside cultural differences, the country's regulatory efficiency and favorable tax environment are key draws for Chinese investors. With China's growing global influence, particularly through the Belt and Road Initiative, Luxembourg's strategic location in Europe has made it a vital entry point for Chinese capital, reinforcing its role as a crucial gateway for investments between China and the rest of Europe.

The research question this thesis wants to prove is: "What factors have contributed to Luxembourg's role as a significant financial hub for Chinese investments, and what are the wider implications for both nations?" The research focuses on how Luxembourg's economic conversion, financial framework, and forward-thinking policies have placed it central to China's growth in Europe, exploring the impacts on the economy, culture, and geopolitics of this collaboration.

This study focuses on the growing importance of financial connections between China and Europe, as China strives to make its currency more global and strengthen its economic influence in Europe. Luxembourg has emerged as a crucial "middleman" for Chinese financial institutions, providing a secure and advanced setting for international investments. As global finance continues to become more interconnected, Luxembourg's experience offers important insights for other small countries looking to attract foreign investments. The current increase of Chinese financial institutions and investors in Luxembourg, and their impact on the country's financial and cultural scenery, highlights the significance of researching this topic now.

The thesis is organized to provide an overview of Luxembourg's rise as a financial hub for Chinese investments, addressing both the historical and contemporary dynamics of

Sino-Luxembourg relations. It is divided into three chapters, each focusing on a different aspect of the relationship.

The first chapter outlines how, in the 19th century, Luxembourg's economy was primarily agriculture based. Its change started when the country was added to the German Zollverein Customs Union, leading to a surge in steel production, focused on industrial growth. Luxembourg was one of the top steel producers globally for several years. Nevertheless, with the decline of the steel industry in the 20th century, the country shifted its focus to finance. Through engagement in regional partnerships and European commitment, Luxembourg emerged and helped shape modern European economic cooperation and policies. The country has always been open to engagement in European treaties and often, being one of the founders. Luxembourg is a country pro-Europe and holds huge value to its roots. In this chapter, the most attractive attributes of Luxembourg as a destination for Chinese investors are also tackled, with the financial sector and economic performance, multiculturalism, high employment, high GDP, highest quality of life, friendly tax policies and "business-first mentality" being some of the characteristics mentioned. Besides from those, Luxembourg's international trade is depicted, as trade has become increasingly important in its economy.

In Chapter II, the historical, diplomatic, cultural and economic ties between Luxembourg and China, which have been in place since 1911, are examined. The alliance was officially established in 1972 through diplomatic relationships, leading to key events like the creation of Chinese banks in Luxembourg in 1979 and the opening of a Luxembourg Consulate in Shanghai in 2006. This chapter further outlines China's market reforms implemented since 1979 that have strengthened Luxembourg's position in enabling Chinese financial operations in Europe. Foreign direct investment is analyzed thoroughly in this chapter, in which China has taken full advantage of in its economic growth, especially in high-tech industries. Relevant for this scope of study, this chapter delves deeply into Luxembourg's commitment in China's Belt and Road Initiative, counting with two key features: CFL-Chengdu collaboration and Zhengzhou-Luxembourg Air Silk Road.

The third chapter expands on how Luxembourg serves as a financial gateway for Chinese investments entering Europe. Due to its strong regulatory frameworks and beneficial tax policies, Luxembourg has become a center for services denominated in Renminbi, drawing in large Chinese banks. In addition to financial services, Luxembourg has

become a frontrunner in green finance and fintech, positioning itself as an innovative financial hub. Programs such as QFII, RQFII, UCITS, and Stock exchanges have eased greater involvement in accessing Chinese markets and are emphasized heavily. To end the chapter, the current or possible challenges between the countries are tackled with relevance to the international climate we are facing with the geopolitical tensions.

This study aims to hold importance for policymakers, financial institutions, and international investors wanting to operate through Luxembourg. China sees the Grand Duchy as a prime example of how smaller nations can have significant impacts on global financial flows and entry into worldwide markets. Luxembourg's financial system can be used as an example of how it exceeds its expected influence. The results of this study could be used by other small countries aiming to grow their financial industries and draw in foreign investment by implementing new regulations, implement new mechanisms, and carefully positioning themselves towards the international scenery.

On this note, this thesis aims to explore how Luxembourg, a small nation with low population has used its financial knowledge, multicultural environment and regulatory systems to become a key player in China's worldwide financial strategy. In today's globalized society, it is crucial to understand how smaller nations such as Luxembourg can have a significant impact on global finance. To achieve this, the study combines a comprehensive literature review with the analysis of quantitative data, case studies, and on-site research that led to first-hand observation of how industrial complexes laid the groundwork for Luxembourg's economy for centuries.

# **CHAPTER I – LUXEMBOURG’S ECONOMIC FOUNDATIONS FOR CHINESE ENGAGEMENT**

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# 1 Luxembourg's Early Economic Development

## 1.1 From Agriculture to Steel Production

Before joining the European Union (EU), Luxembourg's economy depended on foreign markets and economic cooperation with other countries. In simpler terms, according to *The steel industry and Luxembourg (2024)*, Luxembourg was mainly a farming country with old-fashioned infrastructure and many small businesses that lacked profit.

In 1842, the rural nation transformed as it became a part of the German Zollverein, a customs union<sup>1</sup> (Harmsen & Högenauer, 2020). As *The steel industry and Luxembourg (2024)* mentioned, the Grand Duchy supported a union that allowed Luxembourg to enter the market across the river Rhine, resulting in advantages like importing capital and workers from Germany to Luxembourg. This marked the initial stage of Luxembourg's diverse cultural environment, which is still evident today.

Membership in the Zollverein led to the advancement of the railway system, as indicated by *The steel industry and Luxembourg (2024)*, and laid the foundation for economic expansion. The authors also note that the finding of iron deposits in the south of the nation started Luxembourg's Industrial Revolution. Reinesch (2015) adds, "The Zollverein provided a vast free-trade zone for steel produced in Luxembourg and helped with the distribution of coal, a vital component for making steel. If there had not been economic integration, the steel industry would not have kickstarted the economic growth in Luxembourg and continued to drive the economy for over a hundred years."

Numerous industrial complexes developed in and around Luxembourg City, with a noticeable focus in the south, where their presence can still be seen in villages like Esch-sur-Alzette, Schifflange, and Dudelange (*The steel industry and Luxembourg, 2024*). Another specific case of this presence can be seen in Belval, with "Les hauts fourneaux de Belval" available for public visits that display how steel and iron were produced.

Figure 1, my on-site research, shows some of the industrial complexes that dominated early Luxembourg's economy. These industrial complexes are still predominant in the south part of the country.

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<sup>1</sup> A customs union is an agreement between two neighboring countries that involves removing trade barriers, reducing, or removing customs duties, and eliminating quotas (CFI Team, 2022).



Figure 1 - Industrial complexes in the south of Luxembourg that produce steel/iron. On-site research by me.

Péporté (2022) describes that when Luxembourg joined Zollverein, the country began to industrialize gradually, with other member countries providing resources, export chances, transportation, funding, and workforce. Between 1842 and 1862, German businesses like the Stinnes group and the Gelsenkirchener Bergwerks-AG would make significant investments in Luxembourg steel. Joining the customs union also resulted in new social security laws in 1904 and 1911. These laws covered sick pay, workplace accidents, disability, and pensions and were based on the Prussian model. As per Péporté (2022), this was done to prevent Luxembourg's businesses from being accused of unfair competition by selling lower-priced products at lower prices because they were not paying social security for their employees.

Reinesch (2015) pointed out that in the early 1850s, Luxembourg was still considered one of the poorer areas in Europe due to its dependence on an inefficient agricultural industry. After joining the Zollverein, Luxembourg spurred a period of economic expansion, improving the flexibility of the labor market by attracting both skilled and unskilled workers from nearby areas. This movement was not limited to just external migration. There was a significant labor movement from agricultural regions in the north to industrial centers in the south. These changes prepared the foundation for substantial transformations in Luxembourg's professional environment, as more locals and

immigrants began working in positions like engineers, accountants, and managers, supported by advancements in education and hands-on learning opportunities.

Péporté (2022) emphasizes Reinesch's (2015) words by saying that many Luxembourg residents moved from rural areas to urban centers near the mining region and the outskirts of the capital city. This included immigrants from nearby areas such as the Belgian Ardennes, German Lorraine, Prussian Hunsrück, and Eifel, who made up the labor force in the industrial sector. Many executives and technicians in the steel sector migrated from Germany due to the Zollverein.

Before the wars, Reinesch (2015) reflects that the largest population of foreigners in the country was comprised of Germans and gives us numbers. In 1880, 8,412 people were counted, which accounted for 67.1% of foreign residents. By 1900, the number had increased to 14,931, representing 51.5%; in 1930, it reached 23,576, making up 42.2%; in 1930, it reached 23,576, 42.2%. Additional migrants arrived from afar: Italian laborers accounted for 25% of non-native inhabitants between 1900 and 1950. In 1910, 15.3% of the population were foreign nationals. Over time, this ratio grew significantly and emphasized the idea that Luxembourg has always been a country that appreciates migrants.

By the time World War I was about to start, The steel industry and Luxembourg (2024) praised the Grand Duchy for its achievements as one of the top seven steel producers in the world. In 1911, the authors mentioned multiple companies coming together to create the Acières réunies de Burbach, Eich et Dudelange, important integrated steelworks in those specific villages. This steelwork company built several modern factories and employed in 1913, 3,311 people with 65% being migrants from nearby countries (Belval - Esch Citylife, n.d.).

After World War I ended, Luxembourg faced a crucial historical moment. As Reinesch (2015) notes, the German Zollverein, a vital economic structure for Luxembourg, was disbanded under pressure from the Allies, leaving Luxembourg searching for new economic partnerships. In 1919, a national referendum revealed Luxembourg's strong preference for forming a monetary union<sup>2</sup> with France.

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<sup>2</sup> A monetary union represents a deal between two or more countries and allows the movement of goods, services, currency, and labor across borders (BDC, n.d.).

However, mutual interests needed to align. While Luxembourg sought to maintain its economic stability by aligning with France, France's decision to support Belgium forced Luxembourg to reconsider its strategic alliances. Péporté (2022) elaborates that the end of the Zollverein left Luxembourg's steel industry without its primary market, significantly impacting the national economy.

Reinesch (2015) adds that this realignment led to the creation of the Belgium-Luxembourg Economic Union (BLEU) in 1921 and officialized in 1922. Initially started as a customs union, BLEU evolved into a monetary union by 1935. European Commission (2023) comments that the union adopted the Belgian Franc as the currency of BLEU while conserving the Luxembourgish franc as its national currency.

According to research presented by the Official Declaration: 100 years of the Belgium-Luxembourg Economic Union (2021) in 1921, the BLEU was established as the most advanced level of economic and monetary integration between European sovereign countries, foreshadowing the creation of the Benelux Union, the European Union, and the euro currency.

When BLEU was first established, according to Meade (2009), there were restrictions on how much could be imported. Instead, trade with other countries was mainly regulated through customs duties, and the original 1921 treaty did not deal with limits on the amount of goods that could be traded with other countries.

However, as Meade (2009) notes, things started to change in the 1930s when the Great Depression affected Europe. During this time, Luxembourg began increasingly using import restrictions to help balance its payments and protect its domestic industries from foreign competition. Both Belgium and Luxembourg followed this approach.

Péporté (2022) points out that Luxembourg faced challenges in protecting its local industries, especially agriculture, which had a hard time competing with Belgian agriculture due to size, as Meade (2009) reflects: "... at the time of the formation of the Union the population of Belgium was some 7,500,000 while the population of Luxembourg was no more than 275,000." The union's initial terms were insufficient to help these weaker sectors. This situation showed the complexity of economic integration and the need for careful adjustments to ensure that all parties benefit from the union.

Meade (2009) records that on May 23, 1935, Belgium and Luxembourg agreed to change how tariffs and revenue were assessed, considering the impact on imports and exports and the welfare of consumers and producers. Instead of each country having its own rules, they agreed that the rules would be the same for each party. This change made it easier for goods to move freely between them and fixed the issue. They also decided to manage the money they collected from specific fees on imported goods together.

Early economic partnerships in Luxembourg, such as participation in the Zollverein and establishing a monetary union with Belgium, considerably impacted its cultural landscape. The nation had a large quantity of steel. However, it also depended on coal imports for steel production. With the rise of the steel industry, Luxembourg became not only one of the top producers of steel per person globally but one of the leading producers in overall production. Harmsen and Högenauer (2020) state that while only a small amount of steel produced was used within the country, steel made up 88% of Luxembourg's exports and employed 25% of the working population. The steel industry brought economic change to Luxembourg, leading to cultural exchanges and social integration that shape today's identity.

## **1.2 Luxembourg's European Economic Integration**

According to Harmsen and Högenauer (2020), Joseph Bech, a key figure in Luxembourg's political scene, was instrumental in influencing the country's foreign policy in a new direction. While serving as prime minister and foreign minister for a significant amount of time, Bech recognized the changing global situation and stated his willingness to strengthen control within a European supranational body<sup>3</sup> as early as the 1940s.

After World War II, the Luxembourgish government was crucial in establishing European and global cooperation frameworks. The country abandoned its neutral stance regarding the international climate (CVCE, n.d.).

The Luxembourg Government (2023) clarifies that the nation established the United Nations in 1945, the Organization for European Economic Cooperation in 1948, the Council of Europe in 1949, the North Atlantic Treaty Organization (NATO) in 1949 and the Western Europe Union in 1958. Luxembourg's move to ally with NATO was a significant change from its traditional stance of neutrality, which had been a crucial part

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<sup>3</sup> A supranational organization involves a greater transfer of or limitation of state sovereignty than other kinds of international organizations.

of its foreign policy for a long time. Aside from those, Luxembourg entered a regional partnership which we will see momentarily.

### **1.2.1 Formation of the Benelux Union**

While in exile in London, the governments of Luxembourg, the Netherlands, and Belgium increased their cooperation. This collaboration led to the signing of the Benelux Customs Union Treaty in 1944, as recorded by Harmsen and Högenauer (2020).

The Benelux Customs Union Agreement, as stated in the CVCE Website (n.d.), created a tariff community between the three countries and laid the groundwork for developing an economic union<sup>4</sup> that would enhance economies of scale<sup>5</sup>. As part of this agreement, a standard external tariff was implemented, and customs duties on trade within Benelux were removed, as indicated by the CVCE Website (n.d.).

The Benelux Customs Union started on January 1, 1948, allowing free trade among the three signing countries during a challenging economic period after the war (CVCE Website, n.d.). After the European Defense Community collapsed due to French sovereignty concerns and the changing international landscape with the Cold War, Belgium, the Netherlands, and Luxembourg actively rejuvenated European integration (CVCE, n.d.). Together, they developed a memorandum about economic integration called the Benelux Memorandum, showcasing it at the Messina Conference in 1955 (Fally, 1992).

Despite these ambitions, the path to a complete economic union was difficult, as noted by Harmsen and Högenauer (2020). These challenges were further complicated by differing views on European cooperation, attitudes, and different positioning towards Germany, as well as the utilization of Marshall Plan aid, per CVCE (2016).

Robertson (1956) discusses the inherent economic disparities among the Benelux countries, which were a significant concern. He notes that different economic policies, financial policies, and economic disparities hurt the union's integration efforts. Specifically, the author discusses the Agricultural Protocol, which was primarily

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<sup>4</sup> An economic union is an agreement between two or more nations to allow goods, services, money and workers to move over borders freely. The countries may also coordinate social and financial policies to support this common market (CFI Team, 2024).

<sup>5</sup> Economies of scale involve optimizing productive resources to reduce production costs and ultimately increase the output of goods and services (Loo, 2022).

beneficial to Belgian farmers, highlighting the financial advantages provided to one member state over others due to domestic policy differences. Robertson (1956) also points out the lack of federal ambition within the Benelux agreements and emphasizes that no country had yet to sacrifice the element of sovereignty, suggesting a cautious approach to give national control over economic policies.

Robertson (1956) further highlights those differences by mentioning that indirect taxes created significant legal and fiscal challenges. Belgian producers felt drawn back compared to Dutch producers due to different sales tax rates. Although there was an initial agreement to standardize these taxes, financial difficulties prevented their implementation, showing a reluctance to resolve these discrepancies. Moreover, the author notes that Luxembourg's demand for a shared tax revenue system added complexity to negotiations, illustrating the challenges of aligning tax policies while protecting national revenues.

In October 1949, CVCE (2016) mentions that the three nations agreed to an initial treaty that kept some protective measures in place but allowed for the slow removal of import limits. By July 1953, CVCE (2016) added that the countries agreed to align their economic and social policies. A few months later, the three parties also agreed on a unified trade strategy to handle imports and exports with countries outside their group.

The journey towards an Economic Monetary Union<sup>6</sup> was finalized only in 1958, highlighting the difficulties in aligning the three countries' diverse economic structures and national interests. Benelux's role in broader European affairs solidified as the three countries started to engage independently within the Organization for European Economic Cooperation. Over time, the trio developed a unified voice in global matters, culminating in the signing of the Benelux Economic Union Treaty on February 3, 1958, in The Hague (CVCE, 2016).

According to the CVCE Website (n.d.), this treaty allowed the member states to establish the free movement of people, goods, capital, and services and to collaborate closely on economic, financial, and social policies. The Benelux Union Treaty, established in 1960, was renewed in 2008 and, in recent times it focuses on three key themes, per Benelux Int

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<sup>6</sup> An Economic Monetary Union is a type of trade bloc that features a combination of a common market, customs union, and monetary union. It is established via a trade pact and constitutes the sixth of seven stages in the process of economic integration (Hayes, 2022).

(n.d.): “internal market & economic union, sustainable development and justice & home affairs.” This union influenced the regional economic policies and set a foundational model for what would later mold the European Union.

### **1.2.2 The Schuman Declaration and the European and Steel Community**

Robert Schuman, a French Minister for Foreign Affairs born in Luxembourg, suggested splitting coal and steel resources between France and Germany on 9 May 1950. This suggestion eventually led to the European Coal and Steel Community (ECSC) formation, which represented a significant turning point in the European integration process. Due to Luxembourg's strategic location, it was imperative for the nation to actively participate in these advancements since its future depended mainly on resolving the differences between France and Germany (CVCE, n.d.).

Nevertheless, Harmsen and Högenauer (2020) argue that establishing the ECSC presented a significant difficulty for Luxembourg due to its small size. This was mainly because steel comprised a substantial part of the nation's industrial output (85%) and exports (90%). However, Fally (1992) highlights that Luxembourg was a key player, ranking as the seventh largest steel producer in the world when the ECSC was founded. It was mandatory that Luxembourg participated and complied their national interests with regional policies.

Still, in April 1951, Luxembourg joined the ECSC as one of its six founding members, following EU2015LU (2015). The shift of powers and responsibilities from independent States to a higher-level governing body was a significant advancement. Luxembourg required the coal and steel industry but had substantial worries about removing customs duties on these goods (CVCE, n.d.).

Additional issues highlighted by Harmsen and Högenauer (2020) included concerns about the effects of price competition between member states on social standards in the industry. Luxembourg's salaries were higher than those in Belgium, the Netherlands, and France, sparking concerns about potential competitiveness or wage cuts in the Luxembourg steel sector. Article 31 of the ECSC Treaty was established to alleviate some of these concerns. According to Harmsen and Högenauer (2020), this article permitted the High Authority created by the treaty to manage its finances. Despite these challenges, Luxembourg prevailed, as the nation adapted, complied, and balanced its national interests with regional cooperation.

### **1.2.3 The Path to the European Economic Community**

In 1957, the Treaty of Rome established the European Economic Community (EEC) and the European Atomic Energy Community. As per the Council of the European Union (2021), these advancements were significant. The primary goal of the EEC was to encourage trade and foster integration and economic growth among Belgium, Germany, France, Italy, Luxembourg, and the Netherlands.

This agreement set up the foundation for a single market, enabling the unrestricted flow of goods, individuals, services, and funds. The EEC sought to enhance trade and production conditions among its member states and facilitate closer European political integration (Council of the European Union, 2021). Creating a unified market among the six nations encouraged them to work towards harmonizing their economic policies over time. The development of the single market progressed over time, establishing the foundation for its current structure and functionality.

### **1.2.4 Economy Restructuring post Steel Crisis**

Luxembourg's steel industry was greatly impacted by the global steel market decline during the 1973-1975 recession, as well as the early 1980s recession. Oudendijk (2024) mentions that many factors contributed to the global recession, with the Iranian Revolution being one of them, resulting in a significant increase in oil and energy prices. The author emphasizes that the steel industry was on the verge of destruction and by 1985, the workforce had decreased to 13,400 – a 50% drop from 1974. Danescu (2023) adds that this economic shock caused a significant change in the nation's industrial foundation. Luxembourg, which had benefited from the steel industry during the "Trente Glorieuses"<sup>7</sup>, had to make major structural adjustments.

This restructuring of Luxembourg's economy generally centered around the strategic expansion of the financial zone. The tertiary sector's share of the national economy nearly doubled from 38% in 1958 to 77% in 1995. According to current standards, the service sector contributes 88% of Luxembourg's wealth, with financial services making up a third of this total value (The steel industry and Luxembourg, 2024). Several factors underpinned this remarkable transformation. Luxembourg's economic openness, attractive tax system, and its ability to innovate and adapt quickly played pivotal roles in

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<sup>7</sup> "Trente Glorieuses" are the 30 years post-World War II economic boom (Danescu, 2023).

fostering the growth of the financial sector. These strengths enabled the country to effectively capitalize on opportunities presented by the European single market (Harmsen & Högenauer, 2020).

A key element in Luxembourg's adaptation to modern economic challenges was the Treaty of Maastricht, signed in 1992 and implemented in 1993. This treaty significantly strengthened Luxembourg's role within the European Union, particularly in policy areas such as economic and monetary affairs. As part of the Economic and Monetary Union, Luxembourg had to create its central bank, a member of the European System of Central Banks, which allowed Luxembourg greater financial autonomy than earlier arrangements (Harmsen & Högenauer, 2020).

The Treaty of Maastricht also increased Luxembourg's political influence, which it continued to leverage for both regional and global engagement. Luxembourg's long-standing commitment to European unity is evidenced by its consistent support for European Union policies and its citizens' high levels of European identification. Högenauer (2019, pp. 73-76) notes that Luxembourgers still identify themselves as EU citizens (89%) and the country consistently demonstrates the highest approval ratings for key EU policies, with 96% supporting the free movement of people across the EU. Despite economic difficulties, 85% of Luxembourgers favor the Economic and Monetary Union and the adoption of a single currency.

The Luxembourg Government (2023) highlights that the Grand Duchy's small size has always supported its involvement in shaping Europe. Luxembourg is a diverse country with multiple cultures and languages, brought about by its historical background, geographic position, and population makeup. The Grand Duchy's foreign policy consistently centers around actively engaging in multilateral collaboration regionally and globally. Throughout history, the nation has joined numerous international organizations and institutions, often even being one of the founding members.

### **1.3 Luxembourg's Allure as a Country and to Chinese Investors**

Chinese investors choose Luxembourg as their number one European destination for all sorts of investments and operations. This includes trading, logistics, supervising foreign subsidiaries or permanent establishments, managing foreign real estate, group financing, cash-pooling, risk management, research, and development (R&D), intellectual property, shipping business, e-commerce, and more (Deloitte, 2014). Chinese investment in

Luxembourg has changed the social landscape, especially with Chinese expats promoting cross-cultural understanding and diversity.

Luxembourg's location, economy, and regulatory environment make it very attractive to Chinese investors. In the heart of Western Europe, Luxembourg has access to the major European markets and the EU's consumer base. The country is stable, pro-business, and has a sophisticated financial sector. Plus, Luxembourg is a leader in renminbi<sup>8</sup> (RMB) internationalization, as we will see in detail in Chapter III, and has a diverse multilingual workforce. Here, in this topic and sub-topics, we will go into more detail about Luxembourg's allure as a country and to Chinese investors.

### **1.3.1 Financial Sector and Economic Performance**

Portrait of the Luxembourg economy (2023) states that Luxembourg's economy is highly regarded for its outstanding performance and influence in Europe and globally. It consistently attains top positions in different evaluations of territorial competitiveness, digitalization, and innovation, placing itself in the top 10 countries. While the financial sector plays a vital role in the economy, Luxembourg has made significant efforts to broaden its industries. As a result, it has become a prominent center for logistics and a pioneer in satellite technology and digitalization.

Luxembourg's high level of involvement in the European Union is a critical factor in its success, as shown by its remarkable GDP per capita of 142 billion USD, the world's highest, according to Venditti (2024).

Lloyds Bank Trade (2023a) points out the distinct features of Luxembourg's economy in its analysis, focusing on its financial system and high level of international exposure. The economy of the Grand Duchy is heavily influenced by the financial sector, which accounts for around a third of its GDP. Luxembourg is the world's most prosperous country due to its high GDP per capita. Additionally, it flaunts one of the euro zone's most significant account surpluses. Even though Lloyds Bank Trade (2023a) reported a -0.7% GDP budget deficit in 2022, Luxembourg has consistently kept a strong budget position. Government interventions aimed at reducing the impact of rising energy prices and inflation were the leading cause of this deviation. To address these difficulties, the government implemented multiple assistance programs in the 2023 budget that still take

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<sup>8</sup> Renminbi, or Chinese yuan, is the official currency of the People's Republic of China.

place in the 2024 budget. These actions included lowering fuel and heating oil costs, offering energy subsidies to low-income families, helping businesses impacted by high energy expenses, and introducing a temporary 1% reduction in VAT to foresee decreases in the upcoming years (Lloyds Bank Trade, 2023b).

Despite the projected increase in Luxembourg's public debt to 26% in 2024, it still stands as one of the lowest debt levels in Europe (Lloyds Bank Trade, 2023a). Regarding inflation, in 2023, high energy and food prices mainly drove an 8.4% inflation rate. The International Monetary Fund quoted by Lloyds Bank Trade (2023a) predicts a decline in inflationary pressures in 2024 (3.7%) and 2025 (2.3%), which aligns with the target established by the European Central Bank.

Portrait of the Luxembourg economy (2023) affirms that the financial sector plays a crucial role in the country's gross domestic product, making up 33%. Luxembourg is a central hub for many international financial institutions, strongly emphasizing global operations. The varied and multilingual team effectively handles international operations in private and corporate banking, fund administration and custody, wealth management, and treasury services. Luxembourg has become an essential gateway to the European Union for several non-EU actors, such as the Chinese, providing them with direct entry to the EU's single market region.

### **1.3.2 Why do Chinese Investors choose Luxembourg?**

One of the key advantages of Luxembourg is its strategic geographical location in the heart of Western Europe. Situated between major European cities such as Frankfurt, London, and Paris, Luxembourg is easily accessible by plane or train, with travel times of just an hour or two. Within a 500 km radius of Luxembourg, 40% of the European Union's wealth is concentrated, and this figure increases to 70% if extended to a 700 km radius, as per Deloitte (2014).

Luxembourg provides access to a large consumer market of over 600 million people with high power purchase parity. Consistency and stability in its government and economy are appealing to investors who seek pro-business policies, growth, and success (Deloitte, 2014).

Yves Maas, Chairman of the Luxembourg Bankers Association, confirmed Luxembourg's attractiveness to Chinese investors because of the country's impartiality, business-friendly

regulations, and well-developed fiscal ecosystem (Mironescu, 2017). Luxembourg also hosts the vanguard of green finance and fintech innovations, developed in Chapter III.

On this note, and according to the Ministry of Commerce in China, as quoted by Lam and Tian (2021), over 40% of Chinese investments in Europe are channeled through Luxembourg. The strong connection that the Grand Duchy possesses with China has benefited the local fund industry. In 2024, a staggering 72.1% of European assets<sup>9</sup> invested in China were managed by Luxembourg funds, while 37.6% of global investment funds targeting China were domiciled in Luxembourg, per LFF (n.d.-a) quoting PwC & Lipper (2024). Through the years, China's presence in Luxembourg has expanded, with numerous Chinese banks, private equity firms, asset managers, logistic companies, infrastructure developers, energy companies, and technology firms establishing operations there (Lam & Tian, 2021).

### **1.3.3 Multiculturalism in Luxembourg**

Luxembourg's economic prosperity and ability to withstand challenges can be attributed to its workforce, known for its international outlook, multilingualism, and high level of skills (Portrait of the Luxembourg economy, 2023).

Just Arrived (n.d.) reports that Luxembourg's most significant foreign populations include Portuguese, French, Italian, Belgian, and German inhabitants. Even with many foreign residents, Luxembourg faces few intercultural tensions. This can be credited to a primary aspect of Luxembourg's cultural integration model. The nation's variety demonstrates Luxembourg's commitment to the origin of the Schengen Accords and physically represents the values they support. Efficient communication is crucial in a society where people of various nationalities and cultures interact. Even though Luxembourg officially has three main languages, many others are spoken daily due to the diverse foreign communities residing in the country.

Apart from financial services, Chinese tourists have shown interest in Luxembourg. In 2012, the number of Chinese tourists who visited Luxembourg was reported at more than 160,000 by Luxembourg Government (2013). Eurostat (2018) highlighted the report and stated that the average length of stay of Chinese visitors in Luxembourg was 13 nights,

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<sup>9</sup> Assets are items of value that an individual, company, or organization owns or controls, which can be used to generate income or provide future benefits (Kindness, 2024).

the longest stay compared to other EU-28 countries at that time. The Chinese tourist boom has promoted cultural exchanges and tourism development in Luxembourg.

The University of Luxembourg has established research partnerships with top universities in China, as well as the creation of a language and culture center in Luxembourg, which offers Chinese language courses and cultural activities. Aside from those, it is important to highlight the Confucius Institute's role. They are committed to advancing the Chinese language and culture at the University of Luxembourg, and nationwide, particularly in educational, cultural, economic, and scientific areas. This dedication is viewed as a component of a more comprehensive strategy to deepen mutual understanding and enhance bilateral relations between China and Luxembourg (Luxembourg Confucius Institute, n.d.).

Chinese expats have contributed to Luxembourg's economy and society. Statistics Portal (2023) mentioned that in 2023 there were 4,295 Chinese expats in Luxembourg, which is 5.9% of all foreign expats in Luxembourg. Most of the Chinese expats are in finance and technology, contributing to the economy in these sectors and to economic and cultural development from different angles. They have integrated well into the local business and social dynamics and participate actively in the events organized by the Chamber of Commerce of China in Luxembourg.

Luxembourg's economic location has attracted many people and created a diverse society. This means merging different European communities and international communities, forming a melting pot of cultures. Economic growth has brought cultural diversity and enrichment, along with the values of multiculturalism and social cohesion. As Luxembourg becomes a top financial center, it evolves into a culturally diverse environment. This combination of financial expertise and cultural openness is attractive to global investors, especially from China, and sets the stage for long-term growth and innovation.

#### **1.3.4 Employment and Quality of Life**

Working in Luxembourg Information and advice (n.d.) mentions that the job market in Luxembourg stands out for its diverse international work environment, high number of foreign and multilingual workers, predominant service industry, and lower unemployment rate than the European average. Living and working in Luxembourg (n.d.) highlights that Luxembourg, a democratic constitutional monarchy with a notably open

economy, brings together economic, social, and political stability. The government is crucial in promoting R&D, and innovation initiatives, with various policies stimulating investors and entrepreneurs.

Luxembourg's job market stands out compared to neighboring countries due to higher salaries factoring in taxes and other benefits, linguistic flexibility, and political stability (Lloyds Bank Trade, 2023a). Luxembourg has the highest minimum wage in Europe at 2570.94 EUR for a non-qualified worker over 18 years old working 40 hours a week. Trading Economics (2023) reported the employment rate in Luxembourg stood at 518,061 people (70%). An impressive number considering the population is estimated at 673,036 people as of 2024 mid-year.

Another critical point is the quality of life in Luxembourg, as stated in Numbeo and RankingRoyals (2024). Luxembourg is the top-rated country, not just in Europe but in all other developed nations (see Figure 2). Luxembourg City was ranked the 31<sup>st</sup> most livable city out of 100 cities globally in the Global Livability Index 2024, but 12<sup>th</sup> in European city terms (Global Liveability Index 2024, 2024). Besides that, Luxembourg has a low crime rate and is safe for every type of visit purpose.



Figure 2 - Best Countries for Quality of Life in 2024. Source: Numbeo and RankingRoyals (2024).

### 1.3.5 Tax Policy and Business

In addition to having a higher quality of life than other European and neighboring countries, Luxembourg has a tax system that aims to be fair, sustainable, and competitive. According to Living and working in Luxembourg (n.d.), the amount of taxes paid in Luxembourg depends on household income and size. For instance, based on a scenario presented by the OECD quoted by Living and working in Luxembourg (n.d.), a married couple with two children and two incomes (one at 100% and the other at 67% of the average wage) will have a combined tax and social security contribution of 26%. Indeed, this number has decreased due to a recent tax overhaul, but this is better than the average of 36% in the European Union.

Luxembourg's tax policies, especially those regarding specialized investment funds, have significantly impacted the growth of its financial industry. Kuijk et al. (2012) highlight the importance of tax considerations for Luxembourg's specialized investment funds, making it a desirable location for international financial services. Expanding the financial industry, particularly in sectors such as the renminbi business, has strengthened Luxembourg's position as a top financial hub (LFF, n.d.-b).

Ernest and Young (2017) further highlight:

- Stable tax legislation;
- Access to over 75 double taxation treaties, including agreements to eliminate the taxation of the same income in two countries (i.e. no double taxation);
- Access to all European Union's Directives;
- Easy repatriation of cash to investors;
- No capital duty<sup>10</sup> and no stamp duty<sup>11</sup>;
- 17% VAT;
- Special tax regime for expatriate highly skilled employees (if conditions are met).

In terms of bureaucracy, Luxembourg is known for its light and efficient administrative environment. It is all about “business, not bureaucracy” with streamlined processes and

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<sup>10</sup> No capital duty means that you do not pay taxes when you invest in a company, for instance.

<sup>11</sup> No stamp duty means that you do not pay taxes on certain transactions, such as buying property or shares.

minimal administrative burden. Setting up a legal entity in Luxembourg takes a few days with low capital requirements and fees. The tax administration and filing procedures are easy, Luxembourg also has favorable regulatory regimes and legal frameworks for cross-border trade. Deloitte (2014) adds that the country’s fast-track process and “business-first” mentality means businesses have direct access to politicians and decision-makers. Regular networking events, organized by the government, give leaders and investors the opportunity to meet with officials always looking to support entrepreneurship in the country.

To summarize what has been said thus far, Figure 3 highlights the important aspects covered by these sub-sections, while refuting Luxembourg’s best qualities as a country and allure to Chinese investors.



Figure 3 – Luxembourg factors of appeal to Chinese investors. Source: Deloitte (2014).

## 1.4 Luxembourg's Role in International Trade

Lloyds Bank Trade (2023b) depicts Luxembourg's international trade. The same writer points out that Luxembourg, because of its petite size and strategic position, displays an impressive willingness to engage in foreign trade, with a surprising 388% of its GDP coming from this industry. The country mainly focuses on exporting business services, specifically the finance sector. The main export categories include metals (23.4%), machinery (18.2%), other manufactured goods classified by raw materials (15.5%), and transport equipment (10%).

On the other hand, machinery (16.5%), transport equipment (15.9%), chemicals and related products (12.8%), and mineral fuels (9.3%) are the main categories of imports as reported by Lloyds Bank Trade (2023b) citing from Statistics Luxembourg.

Luxembourg relies on its European Union partners for its economic operations. 92.5% of the products imported in 2022 originate from other member states, with exports accounting for 88% of the overall total. Over 50% of its trade is with neighboring countries (Lloyds Bank Trade, 2023b). Th25

largest customers for Luxembourg are Germany, France, Belgium, and the Netherlands, with exports surpassing one billion USD. Luxembourg tends to import from those same countries, and recently, China has been an active key player in Luxembourg's imports, accounting for 759,644,411 USD (Luxembourg: Trade Statistics, n.d.).

The data shown in Figure 4 from OECD (n.d.) illustrates that Luxembourg holds a prominent position in export and import levels relative to its GDP. In 2022, Luxembourg had the highest export value relative to its GDP, reaching an impressive 211.28%. This shows that the value of Luxembourg's exports is more than twice as large as its GDP. Compared to other nations, Luxembourg's export performance is outstanding. Its economy is highly open and export-oriented, as evidenced by its exports significantly surpassing its GDP. Luxembourg is also ahead in imports compared to its GDP, with a percentage of 177.24% in 2022, demonstrating a very open economy with extensive trade.

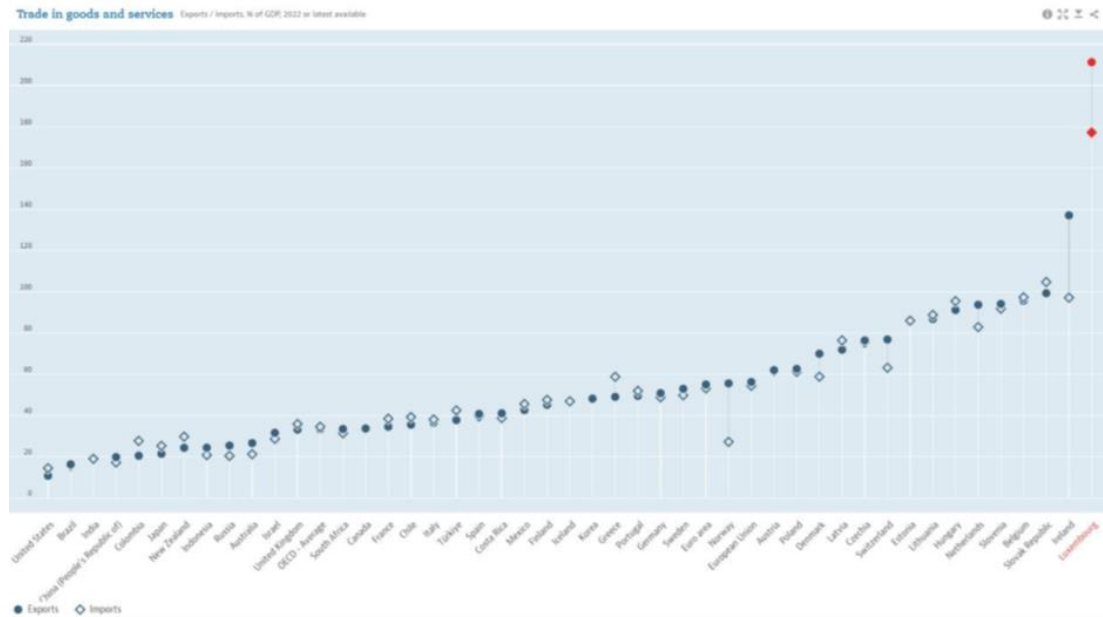


Figure 4 – Trade in goods/services. Exports/Imports % of GDP, 2022 or latest available. Source: OECD (n.d.).

Luxembourg's goal is to boost its trade alliances with Asian nations, primarily China, as seen before with the number of Chinese expatriates and businesses in Luxembourg, and the potential for improvement. This topic will be developed further in Chapter II, when “Bilateral Trade with Luxembourg” is mentioned.

## **CHAPTER II – LUXEMBOURG AND CHINA’S JOURNEY FROM DIPLOMACY TO ECONOMY**

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## 2 Timeline of Diplomatic and Economic Relationship

According to Luxembourg Government (2013), the economic relationship between China and Luxembourg started in 1911. Eugène Ruppert is the figure who highlights this aspect. As a Luxembourgish engineer, he introduced the first blast furnace at the Hanyang Iron Plant in Wuhan after arriving in China in 1894, marking the beginning of China's modern industry.

Luxembourg Trade and Invest (2020) presents us with a roadmap that depicts the development of all the relationships between the countries. As a reliable source, Figure 5 and future reference authors show all the crucial events that led to cooperation over the years.

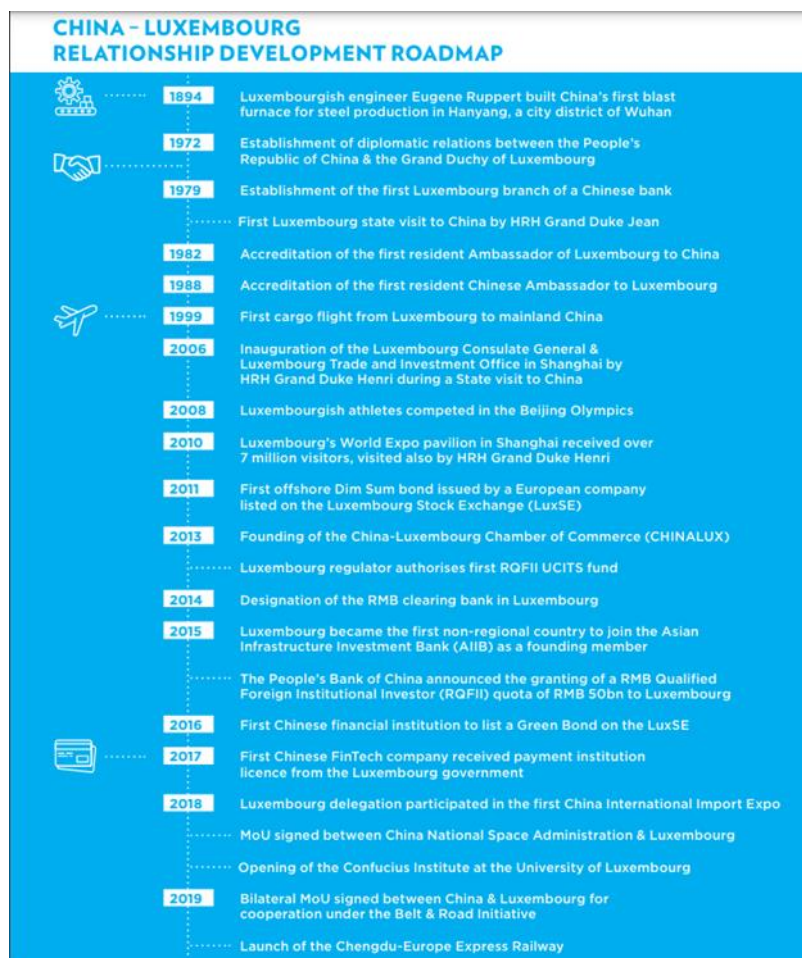


Figure 5 – China-Luxembourg relationship development roadmap. Source: Luxembourg Trade and Invest (2020).

Official diplomatic relations between nations started in 1972. Years later, in 1979, the same research timeline includes the establishment of the first overseas branch of a

Chinese financial institution in Luxembourg (Bank of China). This turning point event marked the beginning of cooperation and commitment to a positive partnership.

In the 1980s, the diplomatic relationship between China and Luxembourg strengthened as the first resident ambassadors were officially recognized. Luxembourg assigned its first ambassador to China in 1982, and China settled its first ambassador to Luxembourg in 1988. These diplomatic achievements served as a basis for their political and economic relations.

Kurzawa (2021) emphasizes: "Although China and Luxembourg differ in size, population, social system, and level of development, our two countries both adhere to the principles of mutual respect, mutual equality, and win-win cooperation, always considering each other as important partners and insisting on strengthening dialogues and properly managing differences. Since the establishment of diplomatic relations between our two countries 50 years ago, bilateral exchanges and cooperation in various fields have been developing more and more profoundly, and the friendship between our two peoples has been strengthening day by day. All this has laid a solid foundation for the further development of Sino-Luxembourg diplomatic relations."

The spirit of cooperation has continued to define China-Luxembourg relations, as demonstrated by subsequent milestones. For instance, in 1999, a significant achievement occurred in trade when the first cargo flight from Luxembourg to mainland China took place. This development led to a boost in product exchange between the two countries, a momentous event still recognizable today.

In 2006, Luxembourg increased its presence in China by establishing the Luxembourg Consulate General and Luxembourg Trade and Investment Office in Shanghai. This project, initiated by Grand Duke Henri during an official trip, sought to increase trade and investment between the two countries. Luxembourg athletes' involvement in the 2008 Beijing Olympics illustrated the strong cultural exchange bond between the two nations.

Luxembourg's pavilion at the 2010 Shanghai World Expo was a great success, attracting over seven million visitors and fostering greater cultural interaction. CC (2012) highlights that the event significantly boosted Luxembourg's profile in China, with the pavilion becoming a major attraction, particularly due to the presence of the Gëlle Fra (Golden Lady) statue.

In 2011, a significant advancement in financial collaboration occurred when a European firm became listed on the Luxembourg Stock Exchange (LuxSE) and brought the inaugural Dim Sum bond<sup>12</sup>, issued outside of China's mainland. In 2012, CC (2012) added that the Hereditary Grand Duke Guillaume and Hereditary Grand Duchess Stéphanie officially visited China, marking their first visit abroad after their wedding. With this gesture and the presence of the Luxembourg trade delegation, led by the ex-Minister of the Economy and Foreign Trade, Etienne Schneider, the visit also marked the 40th anniversary of diplomatic relations between Luxembourg and China.

In 2013, the Ministry of Foreign Affairs of the People's Republic of China (n.d.) mentioned that interactions in trade and learning likewise became more established throughout the year. New units were formed in February 2013 by establishing the Chinese Language and Cultural Center in Luxembourg. In the exchanges, the "art troupe" known as Cultures of China, and the Festival of Spring went to Luxembourg to perform. In April of the same year, the Luxembourg film delegation attended the Third Beijing International Film Festival.

Still, in 2013, we saw the establishment of the China-Luxembourg Chamber of Commerce and Luxembourg's approval of the initial Renminbi Qualified Foreign Institutional Investor (RQFII) Collective Investment in Transferable Securities Directive 2009 (UCITS) fund, which established additional advancements in monetary integration. These topics are crucial to understanding this work and will be explored.

Luxembourg made history in 2015 as it became the first non-nearby country to join the Asian Infrastructure Investment Bank (AIIB) as a founding member. That same year, Luxembourg was allocated a RMB 50 billion quota for the RQFII program, facilitated by the People's Bank of China (Luxembourg to become the first European founding member of the Asian Infrastructure Investment Bank (AIIB), 2015). This marked an important step toward deepening financial cooperation with China.

In 2016, a tremendous event occurred when a Chinese monetary organization issued a Green Bond on the LuxSE, demonstrating their determination to sustainable finance. In the fintech sector, a Chinese company made significant developments in 2017 when it obtained a payment institution license from the Luxembourg government. Luxembourg

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<sup>12</sup> A bond is a way to invest money by giving it to a government or company for a certain time. You earn regular interest and get your money back when the bond ends (Fernando, 2024).

was also involved in the first China International Import Expo in 2018, signed a Memorandum of Understanding (MoU) with the China National Space Administration, and opened the Confucius Institute at the University of Luxembourg.

In 2019, Luxembourg and China signed a joint MoU and launched the Chengdu-Europe Express Railway to fortify trade exchange as a part of the Belt and Road Initiative collaboration, further explored as a case study. Throughout history, those significant achievements show off the developing bond between the two, characterized by using robust economic ties, cultural exchanges, and strategic partnerships.

## **2.1 China's Economic Transformation**

Balmas et al. (2022) inform us that China is undergoing significant structural economic and political reforms. According to the International Monetary Fund et al. (2004), China's transition into a vibrant economy driven by the private sector and its assimilation into the global economy have emerged as some of the most remarkable economic advancements in recent times. Indeed, we have all heard of the "Chinese miracle" in the media. The economists attribute the fast economic sprout of China to primarily three factors: high capital investment, foreign investment, and high productivity rates. These have been crucial in driving China's phenomenal economic miracle.

It is undeniable that China's strength lies in its economic power. Lin (2011, p. 3) adds: "China's growth in the global economic scene over the past two decades is unprecedented." The same author adds that "...it is an extraordinary contrast to the modest performance of other transitioning economies in Eastern Europe and the former Soviet Union" (Lin, 2011, p. 3). In this regard, Wayne Morrison, quoted in Congressional Research Service (2019), informs us that "China is currently the world's second-largest economy, the largest exporter of goods, the second-largest importer of goods, the second-largest recipient of foreign direct investment, the largest manufacturer, the largest holder of the foreign exchange reserves, and the largest creditor nation in the world."

Congressional Research Service (2019) reflects that before 1979, China, led by Chairman Mao Zedong, adhered to the centrally planned economic system. The Investopedia Team (2020) notes that this system occurs when the government makes necessary economic decisions concerning the production and distribution of commodities. In centrally planned economies, decisions are centralized rather than arising from the individual choices of producers and consumers, as in market economies. The Chinese state played a significant

role. They directed and regulated substantial portions of the nation's economic output. They established production targets, controlled prices, and allocated resources across various sectors of the economy.

China began reforming and “opening up” the economy in 1979, according to Congressional Research Service (2019). The central government provided local farmers with an incentive that involved a shift in ownership and pricing. The farmers had an opportunity to dispose of small amounts of the farm produce in the open market. The government set up four special economic zones along the coast. They were meant to encourage foreign direct investment, foster exports, and import advanced technology products into China. The technological advancements in China are clear, and these developments can be traced back to the series of reforms that have taken place in the country.

These reforms were introduced slowly. They were meant to improve economic policy, especially in trade, fight the control of successive small organizations from the central government, and delegate it downwards to the provincial and local authorities, allowing those to operate and produce essentially based on market principles. However, people were also encouraged to start their own companies. A few coastal areas and cities were opened and labelled as open cities and development zones, allowing them to experiment with free-market reforms and give tax and trade incentives to attract foreign investment (Congressional et al., 2019).

China’s economic success can be attributed to the excellent job trade liberalization<sup>13</sup> has done. The author further describes that these entail schedules of prices, such as taxes and other charges, and nontariff barriers like regulations on licensing and quotas on imports.

The removal of trade barriers facilitated greater competition and encouraged foreign inflows of direct investments to China. China's gradual economic reform aimed to identify successful policies that provided favorable financial returns. This process, described as “crossing the river by touching the stones” by Deng Xiaoping, indicated closer assessment and application of successful policies in various regions of the nation (Congressional et al., 2019). China’s high economic growth has also significantly influenced its cultural identity and social model. The nation’s inclination towards

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<sup>13</sup> Trade liberalization entails removing or reducing barriers to facilitate the free flow of goods between countries (Banton, 2021).

international trade and investment has facilitated cultural exchange, promoted social practices, and contributed to a more globalized society in China.

## **2.2 Foreign Direct Investment in China**

Foreign Direct Investment (FDI) is when an investor from one country acquires a significant stake and control in a foreign business, usually comprising over 10% of voting shares (OECD, 2023). It is an effective mechanism for promoting the worldwide interconnectedness of economies, enabling the exchange of technology, commerce, and sustainable economic partnerships. It also stimulates economic growth through strengthening relationships between countries.

For the past ten years, China has been the recipient of the second-highest amount of foreign direct investment globally, with approximately 189 billion USD attracted in 2022 (CGTN, 2023). FDI inflows were strong at the beginning of the COVID-19 pandemic but began to decrease in mid-2022 and have continued to do so in 2023 and 2024 thus far.

### **2.2.1 Evolution of Foreign Direct Investment Landscape**

China's economy has greatly benefited from its growing acceptance of foreign direct investment as well as international trade. FDI started increasing in the 1970s and peaked in the 1990s when China became the leading recipient of FDI in the developing world because of its significant market, cheap workforce, and modern infrastructure. Tax breaks and the creation of special economic zones were crucial in luring foreign investors, according to Tseng (2003). As per the Congressional Research Services (2019), China's strategy for modernization and development in the 1980s and 1990s was centered on encouraging FDI to boost domestic growth and enhance industrial capabilities.

Despite progress in attracting foreign investment, China still faces obstacles such as regional inequalities, corruption, and geopolitical tensions that hinder the complete utilization of FDI. Throughout history, 88% of foreign direct investment has been drawn to the eastern regions due to their advanced infrastructure, close access to global markets, and strong connections with Chinese communities abroad. In 2000, the Chinese government implemented the "Western Development Strategy" to fix these disparities by improving infrastructure and creating better conditions for FDI in inland and western areas (Taube & Ögütçü, 2002).

Foreign direct investment has been crucial in fueling China's economic expansion and advancements in technology. European multinational companies, specifically in sectors such as electronics and telecommunications, have facilitated China's access to top-end technologies and enhanced its international influence (Duarte, 2014, pp. 180-186). Despite progress made, FDI has been decreasing since 2011 because of stricter regulations, more competition at home, and external factors like geopolitical tensions and the COVID-19 pandemic. After increasing by 20.2% in 2021, FDI decreased to 8% in 2022 and further dropped by 8% in 2023 (Interesse, 2024).

To address these difficulties, China implemented a recent Foreign Investment Law in 2020, to improve the investment environment by prohibiting compulsory technology transfers, safeguarding intellectual property rights, and guaranteeing equitable treatment for foreign investors. Moreover, the government implemented "negative lists" to specify sectors available for foreign investment and created more special economic zones to lure global capital (Statista, 2023).

Progress in internet connectivity, telecommunication, and technology funding has positively impacted the inflow of foreign direct investments, particularly in less-developed urban regions. Zhang et al. (2024) argue that these advancements illustrate China's commitment to leveraging digital transformation to draw foreign investments into less developed regions.

Hong Kong continues to be a major entry point for FDI into China, representing approximately half of FDI inflows in 2022. Being a prominent financial hub, Hong Kong redirects investments from different global origins into mainland China. According to data from UNCTAD in 2020 quoted by Interesse (2024), Hong Kong constituted 10.4% of China's foreign direct investment, while the United States accounted for another 10.4% and Chinese companies outside of mainland China contributed 12.1%. Even with the recent decrease in FDI inflows, China still stands out as one of the leading global FDI destinations. High-tech manufacturing and modern services remain the top sectors, fuelled by Asian countries' demand, with Hong Kong playing a crucial role.

China's latest policy measures like the Foreign Investment Law and new Special Economic Zones seek to create a more welcoming investment climate by encouraging renewable energy, safeguarding intellectual property, and facilitating international data exchange. This shows China's dedication to maintaining an appetizing environment for

foreign investors (Interesse, 2024). With the ongoing development of digital infrastructure, China's attractiveness to investors increases, especially for those seeking technologically advanced and accessible markets. China's strategic location and business-friendly policies, along with its continued focus on digital infrastructure, establish China as a key player in the worldwide investment scene (Nikkei Asia, 2024).

## **2.2.2 Policies to attract Foreign Direct Investment**

China has implemented numerous strategies to attract foreign investment and ensure the stability of the global supply chain. In 2023, the State Council implemented 24 strategic initiatives divided into 59 specific components to improve the appeal of the environment for foreign investment. These measures focus on various aspects such as enhancing foreign firms' entry into industries like high-tech and biomedicine, reinforcing copyright protections, providing tax incentives, and ensuring fair treatment in government purchasing procedures (China Daily, 2023).

The 24 principles are meant to offer a strategic structure for these goals, while the 59 additional actions outline practical procedures for carrying them out, including creating "green channels" for urgent data exchanges and enhancing regulatory support for investment in central and western areas. This method supports China's aim for equal regional growth by allowing international investors to discover alternative operational centers beyond the usual economic hubs (Begum, 2024; Mingyang, 2023; China Daily, 2023).

China's large economy, industrialized environment, and rising middle class continue to make it attractive to foreign investors (Begum, 2024). The eastern regions' success, due to proximity to global markets, developed infrastructure, and the establishment of special economic zones with preferential tax regimes, has also created a self-reinforcing cycle of development that continues to attract more FDI (Taube & Ögütçü, 2002).

## **2.3 China's Foreign Trade**

Santander Trade (2024) reflects that China is the world's biggest exporter and second-largest importer, with a massive trade surplus. Despite its strict regime, China appears relatively open to foreign trade. 2022 trade accounted for 38.4% of its GDP (MacroTrends, 2024). China primarily exports and imports electrical and electronic products, machinery, furniture, plastics, toys, and transport vehicles. The United States,

European Union, Hong Kong, Japan, South Korea, Vietnam, Australia are the key trade partners of China.

Santander Trade (2024) further emphasizes that trade has grown increasingly vital to China's overall economy and is currently considered one of the primary instruments of economic modernization in China. The same author quotes the World Trade Organization's report to add that in 2022, the gross value of exported goods reached 3,593.5 billion USD while that of imported goods was 2,716.1 billion USD. In 2022, China exported services worth 465 billion USD and imported services worth 424 billion USD. Notably, China's export and import growth rates showed an astonishing 40% and 16% surge in 2022 (Figure 6).

Foreign Trade Values	2018	2019	2020	2021	2022
Imports of Goods (million USD)	2,135,748	2,078,386	2,065,964	2,686,747	2,716,151
Exports of Goods (million USD)	2,486,695	2,499,457	2,589,952	3,358,163	3,593,523
Imports of Services (million USD)	525,154	500,680	381,088	426,998	465,053
Exports of Services (million USD)	271,451	283,192	280,629	392,198	424,056

Figure 6 – Foreign Trade Values China from 2018 to 2022. Source: Santander Trade (2024).

### 2.3.1 Bilateral Trade with Luxembourg

Now, let's talk about the current year. In March 2024, China exported 29.6 million USD worth of goods to Luxembourg and imported 27.7 million USD from Luxembourg, resulting in a positive trade balance of 1.92 million USD, according to OEC (2024). Comparing with the data over the year from March 2023 to March 2024, Chinese exports to Luxembourg dropped by 5.31 million USD (-15.2%) while imports from Luxembourg went up by 1.99 million USD (7.74%).

The top exports from China to Luxembourg were refined petroleum (15.4 million USD), delivery trucks (4.24 million USD), computers (3.93 million USD), and rubber working machinery (2.98 million USD), according to OEC (2024). As for imports, the leading commodities China imported from Luxembourg were non-woven textiles (2.99 million

USD), polyacetals (2.8 million USD), valves (2.76 million USD), copper foil (2.3 million USD), and iron railway products (1.45 million USD), per OEC (2024).

In March 2024, OEC (2024) reported that Luxembourg's exports to China decreased mainly due to significant falls in shipments of laboratory reagents (down 12 million USD or -93.2%), telephones (down 1.4 million USD or -85.9%), and semiconductor devices (down 767,000 USD or -57.9%). However, the increase in China's year-by-year imports from Luxembourg was mainly driven by a rise in product imports of other measuring instruments (up 484,000 USD or 99%), polyacetals (up 467,000 USD or 20%), and valves (up 254,000 USD or 10.2%).

The current export of Luxembourg to China is relatively small, but it has spread into different goods and services. The significant imports recorded by China from Luxembourg include polyacetals, measuring instruments, and electrical machinery. Polyacetals have various uses, most of which are in manufacturing home appliances, automobiles, and engineering goods. Measuring instruments can be classified as research and scientific instruments in laboratories and analysis. Luxembourg's exports from China include refined petroleum and machinery, pointing to China providing essential goods. This trade highlights that China is willing to look for more partners and have a balanced, round "positive trade", even with smaller countries.

## **2.4 China's Strategic Trade**

China has signed Bilateral Investment Treaties with more than 100 nations, including Austria, Belgium, Luxembourg, Canada, France, Germany, Italy, Japan, Korea, Spain, Thailand, and the United Kingdom (TradeGov, 2023). TradeGov (2023) also notes that China has entered into 17 free trade agreements with its trade and investment partners and is implementing eight more. Some of China's free trade agreement partners include ASEAN countries, Pakistan, New Zealand, Chile, Peru, Costa Rica, Iceland, Switzerland, Maldives, Mauritius, Georgia, South Korea, Australia, Hong Kong, and Macau.

To deepen its regional economic ties, China joined the Regional Comprehensive Economic Partnership (RCEP), the world's largest trade agreement by GDP, on January 1, 2022. Signed in November 2020 and ratified by China in early 2021, the RCEP encompasses ASEAN member states along with China, Japan, South Korea, Australia, and New Zealand. Together, RCEP countries account for around 30% of the global GDP and represent half the world's population (TradeGov, 2023).

The RCEP Agreement mentions that its purpose is to fashion a high-quality and mutually beneficial economic partnership for the additional development and prosperity of the peoples of this region and others by enhancing the market and productivity opportunities for businesses and investors and by supporting the multilateral trading system in a liberal, non-discriminatory way (ASEAN, 2020).

#### **2.4.1 Recent Trade Performance**

Thus far in 2024, China's total imports and exports increased by 8.7% year-on-year in yuan terms (Xinhua, 2024). According to official statistics from the General Administration of Customs quoted in Xinhua (2024), the country's total foreign trade from January to February reached 930.96 billion USD. Of this, exports were 527.37 billion USD, up 10.3%, while imports reached 403.59 billion USD, a 6.7% increase compared to the same period in 2023.

Private enterprises played a key role in this growth, accounting for 54.6% of the total trade value, which is 4.2% higher than before. Foreign-invested companies contributed 29% of the total trade (Xinhua, 2024).

Trade with ASEAN countries grew significantly, with a total value of 138.47 billion USD from January to February, up 8.1%, making up 15% of China's total trade. However, trade with the European Union, China's second-largest trade partner, decreased by 1.3% (Xinhua, 2024).

China's exports were mainly machinery and electronic products, which made up nearly 60% of total exports. Notably, the value of exports in automatic data processing equipment rose by 7.3%, integrated circuits by 28.6%, and vehicles by 15.8% (Xinhua, 2024).

#### **2.5 The Belt and Road Initiative**

The Belt and Road Initiative (BRI) has become a prominent topic in conferences, centers, forums, funds, and various activities related to its implementation. Xi Jinping officially introduced the BRI in 2013.

According to Carrai (2023), the BRI pursues several goals for China, encompassing domestic and foreign policy dimensions. Primarily, it is a strategy to increase China's security as an emerging global actor and claim its proper place globally. Despite a

contentious debate in China over the nature of the BRI project since its inception, it is widely seen by Chinese observers and scholars as more than just an economic “initiative”; rather, it is seen as a substantial “strategy.” However, the current government has stated that a proper title for it is an initiative, not a strategy. The objective is to create a single transport communication over a network connecting Eurasia with Asia, Europe, Africa, and Latin America through investment in infrastructure across these regions, emphasizing Asia.

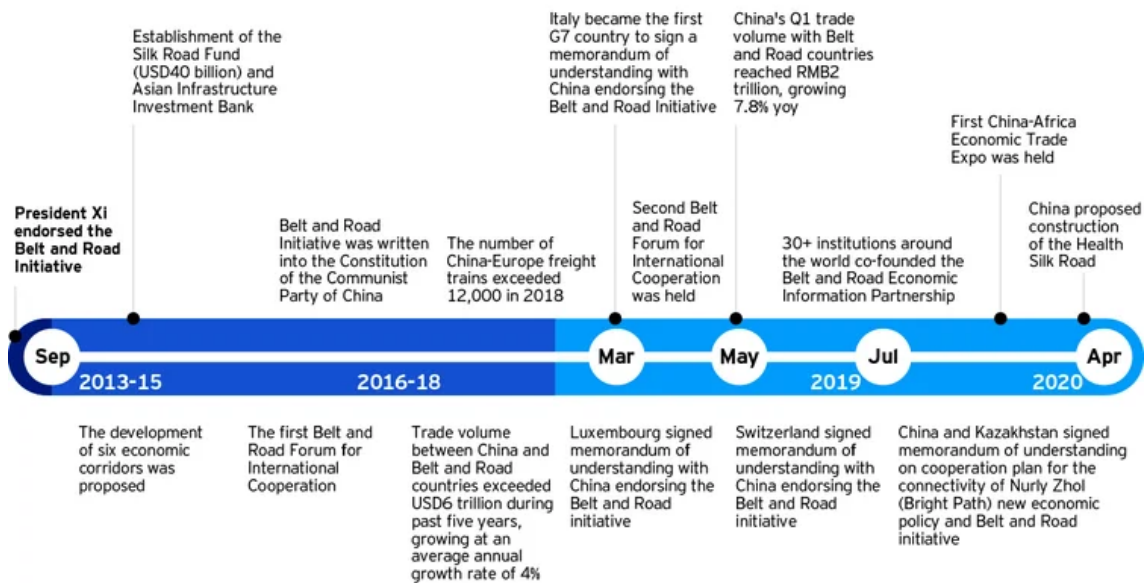


Figure 7 – Belt and Road Initiative Milestones timeline. Source: Invesco (n.d.).

Carrai (2023) states that the BRI aims to help developing countries achieve faster growth, transformation, and shared benefits, fostering broader inclusive globalization. Investments in railways, highways, ports, energy, and telecommunications increase trade volume and bring countries closer. From 2013 to 2018, China’s trade with BRI countries surpassed 5 trillion USD, and foreign direct investments exceeded 70 billion USD (Carrai, 2023).

### 2.5.1 Spread of the Initiative

Initially described as regional infrastructure projects, the BRI has grown exponentially and become a key theme of China’s 13th Five-Year Plan (2015-2020). This plan includes financial integration, trade liberalization, people-to-people exchanges, and creating a “digital silk road.” Gang (2021) argues that enhancing financial integration is a crucial assurance for the Belt and Road Initiative. Using the renminbi can effectively lower

exchange costs for other countries in the initiative and strengthen their ability to mitigate financial risks.

The BRI connects China to the European continent, relieving chronic excess capacity and enabling Chinese firms to gain international experience in various sectors. From the Chinese perspective, the BRI enhances China's presence in Central Asia, the Middle East, and Europe (Carrai, 2023).

Le Corre (2023) highlights that Luxembourg and Switzerland officially endorsed the BRI in April 2019, following Italy, which became the first G7 country to endorse the BRI in March 2019. However, most Chinese foreign direct investments are directed towards significant economies that have not officially supported the BRI. The United Kingdom, Germany, and France received the largest share of Chinese FDI between 2000 and 2018. As Le Corre (2023) outlined, the divergence shows that signing the BRI MoU does not necessarily lead to higher inflows of Chinese FDI.

Moreover, China has gathered support through thematic conferences such as the Belt and Road Forums in 2017 and 2019 in Beijing, where Luxembourg representatives and many European leaders were present. The involvement of Luxembourg officials at these high-level forums points to Luxembourg's active participation in BRI's diplomatic and cooperative efforts.

This broad expansion sets the stage for various countries, including Luxembourg, to engage with the BRI in unique and significant ways, leveraging their strategic positions to enhance regional and global connectivity.

### **2.5.2 Luxembourg's Commitment to Belt and Road Initiative**

Brattberg and Soula (2018) depict that Luxembourg is instrumental in the growing Chinese investments in Europe. It is not, however, connected to the Belt and Road, and the region continued to experience a steep rise in Chinese foreign direct investment. By 2016, Chinese accounts in Europe had registered 35 billion EUR, compared to less than 1 billion EUR in 2008, as money mainly flew from China to Europe instead of the other way round. This impressive growth alone is a testament to the increasing attractiveness of Europe as a significant target geography for Chinese capital flows. This is one of the reasons why Luxembourg is part of the hands in BRI, as it is the second European country on board.

Luxembourg exploits its participation in the BRI by positioning itself as an international financial center, thereby creating solid global links with China, which can be substantiated by specific accords and synergies aiming to bolster the economic and logistical integration processes between the two nations. Following the signing ceremony held at the Boao Forum, the Luxembourg Stock Exchange went into several agreements with Chinese financial institutions (OBOREurope, 2019). These included:

- Agreements with the Shenzhen Stock Exchange and Shanghai Stock Exchange regarding requests to collaborate in the development of trade in green finance products;
- Cooperation with the Shanghai Clearing House, creating a mechanism for LuxSE to access the China Interbank market (domestic bond market);
- Both LuxSE and Bank of China have finalized an agreement to help bring the Chinese bank into the role of facilitator between the Chinese and European markets through financial intercommunication.

Luxembourg's wealthy success can be directly attributed to its commitment to European integration and open requests. This has created a remarkably close relationship between Luxembourg and China, as China sees Luxembourg as a perfect gateway to Europe. Luxembourg's early joining of the European Union has always contributed to developing China-EU relations (China Embassy, 2022).

Former Deputy Prime Minister of Luxembourg Etienne Schneider said the country is hungry to receive Chinese investment and has been positioned as the most appropriate European paradise. Schneider also confirmed Luxembourg's strategic goal of attracting Chinese investments and integrating them into the European project (Luxembourg fully supports China's Belt and Road Initiative: Deputy PM, 2018).

The "One Belt, One Road" action has strengthened the China-Luxembourg relationship. The ChinaLux Chamber of Commerce, in cooperation with the Chamber of Commerce and the Cluster for Logistics, holds forums to discuss mutual gains and share logistics gests. Pierre Gramegna, former Luxembourg's Finance Minister, made remarks during the event emphasizing the government's sweats to get all the belts of the BRI and work it in favor of Luxembourg (Mironescu, 2017).

During these discussions, Gramegna quoted in Mironescu (2017) highlighted the possibility of green finance, adding that China and Luxembourg cooperate in this domain.

In October 2017, the Industrial and Commercial Bank of China launched the first climate bond related to BRI systems on the LuxSE. Also, China Everbright Bank received authorization to establish an attachment in Luxembourg. This was the seventh Chinese bank to have done so.

While Chinese FDI has generally declined in Europe, investments have been recorded in other EU countries, including Luxembourg, as per Le Corre (2023). This development shows a strategic asset diversification, targeting major and minor economies. Luxembourg looks forward to engaging with China's growth, underscoring its critical function in promoting profitable Sino-European relations.

Luxembourg's participation in the BRI has also created possibilities in fiscal services. Mironescu (2017) mentions that Luxembourg is critical to developing into a significant mechanism for Europe and Asia, enhancing trade and budgetary operations, and adding the renminbi. Advanced connectivity across Eurasia is expected to boost global trade and create new jobs. Gramegna, quoted by Mironescu (2017), pointed out Luxembourg's stability and trustability as a partner within the BRI framework.

### **2.5.3 Case study: CFL Multimodal and Chengdu International Railway Service Co. Collaboration**

One of the key elements of Luxembourg's involvement in the BRI is the partnership with Chengdu International Railway Service Co. (CDIRS) on supply chain connectivity through combined train services. This connects the Intermodal Terminal of Bettembourg-Dudelange in Luxembourg to the Chengdu Qingbaijiang International Railway Port in China.

Like CP in Portugal, CFL, or Société Nationale des Chemins de Fer Luxembourgeois, is Luxembourg's national railway company. It is a monopoly. CFL offers free domestic trains for daily needs and paid international trains. This is another way Luxembourg positions itself in the BRI and global trade through rail.

In 2019, CFL multimodal and CDIRS launched a combined train service between Bettembourg-Dudelange and Chengdu Qingbaijiang. The first train left Luxembourg on April 4, 2019, and arrived in Chengdu on April 19, 2019, traveling over 10,000 km through Germany, Poland, Belarus, Russia, and Kazakhstan. This was a test run

facilitated by CDIRS with the involvement of RTSB<sup>14</sup>, and CFL multimodal to establish a weekly service for customers (Büchler, 2019).

Unfortunately, the ambition to have a regular Luxembourg-China rail link did not materialize. Despite the initial success, no trains have run on this route since the test runs in 2019. Barbara Chevalier, Director of Strategy and Development at CFL Multimodal, explained there was no market demand for direct lines. CFL focused on the Bettembourg-Poznan connection in Poland, which has been running twice weekly since early 2020. Trade between Luxembourg and China is now routed through Poland, and the Bettembourg-Poznan line is a critical link in the supply chain (Obert, 2022).

The short-lived success of the direct Luxembourg-China train link indicates that international logistics are a volatile affair. This sector needs to adapt quickly to market demands and consider political realities. The business remains willing and able to deal with obstacles, reflecting Luxembourg's flexibility and strategic stance as part of the BRI, even though the direct route to Chengdu is history.

#### **2.5.4 Financial Cooperation and Opportunities**

China and Luxembourg fortified their cooperation more than ever in 2019 via the Belt and Road Initiative. Cao (2019) points out that both sides have made concrete commitments to each other in financial sector cooperation. This occurred during the meeting between China's ex-Prime Minister Li Keqiang and Luxembourg's Vice Prime Minister Xavier Bettel. Luxembourg is the "second largest domicile in the world for investment funds targeting mainland China" and "the most prominent European location for renminbi bond listings" (LFF, n.d.-a). The country's former Minister of Finance, Pierre Gramegna, when quoted by Mironescu (2017), "Logistics is the most important key success factor for BRI worldwide."

Business representatives discussed opportunities in the BRI after COVID-19 in a ChinaLux conference. James Pomeroy, HSBC London's global economist, refers to China's rapid rebound from the pandemic and the forecast for solid growth because "the BRI can assist other global economies by lifting demand from the Chinese population" (Gerhardstein, 2021). Still, within the same context and Gerhardstein (2021) as a reference author, the ambassador of the People's Republic of China to Luxembourg,

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<sup>14</sup> RTSB is a leading rail freight operator that connects Eurasia.

Xiaorong Yang, stressed that Luxembourg is the second EU member country participating in the BRI. He mentioned that the BRI's goals remain unchanged due to the health crisis as China continues to pursue international cooperation. Yang called for projects under BRI to adopt a digital and green economy. Zhiyao Guo from the Bank of China, Luxembourg Branch, supported the call. He stated that the Bank of China issued over 130 billion USD of credit support for over 600 BRI projects, stressing effective risk management and diversified investment approaches.

Arnaud Delestienne from the Luxembourg Stock Exchange said that international debt capital markets have significant opportunities for BRI. Luxembourg, the second largest fund center in the world, remains a top issuer of bonds and a good platform for BRI project financing. Delestienne, quoted by Gerhardstein (2021) confirmed that Luxembourg knows how to associate international bond issuance. Furthermore, its unique legal structure attracts for funding BRI ambitions.

### **2.5.5 The Zhengzhou-Luxembourg Air Silk Road**

Xinhua (2023) says the Air Silk Road between Zhengzhou and Luxembourg is another essential part of the BRI, connecting China and Europe. This started in 2014 when Henan Civil Aviation Development and Investment Company Ltd. (HNCA) bought 35% of Cargolux, a Luxembourg-based cargo airline, and created the Air Silk Road (Girard, 2018). Since then, this route has expanded to over ten cities worldwide, including hubs like London, Chicago, and Milan.

Rabe and Kostka (2021) point out the uniqueness of the Air Silk Road, driven by Henan's provincial competition and local economic challenges. The Henan provincial government saw the opportunity of Luxembourg looking for a new investor for Cargolux, pushed for economic development in Zhengzhou, and connected the region to the world.

Luxembourg attaches great importance to its bilateral relations with China and is proud of China's development achievements. Khan (2023) says Luxembourg wants to deepen cooperation with China through the Air Silk Road by rapidly developing sectors like finance, environment, and international affairs. Deng Li, quoted by Khan (2023), stresses mutual respect and trust between China and Luxembourg and advocates for multilateral cooperation, cultural exchanges, and mutual learning to strengthen China-EU relations.

The Air Silk Road is in full swing at Cargolux's Zhengzhou hub, where 110 tons of cargo from Luxembourg are processed and 130 tons reloaded in 2.5 hours and delivered to Chicago on time. This fast operation supports cross-border e-commerce and meets the urgent needs of enterprises for quick and reliable transport (Xinhua, 2023).

In 2021, ChinaLux Chamber of Commerce organized a webinar titled 'China and the BRI in 2021 and Beyond' and discussed the future impact of the BRI. The Chinese Ambassador to Luxembourg mentioned the BRI's role in promoting development and international cooperation among Asia, Europe, and other regions. The "Silk Road in the Air" project became more prominent during the COVID-19 pandemic, highlighting the importance of global trade routes (China and the BRI in 2021 and beyond, 2021).

The economic significance of this route is reflected in Cargolux's 2022 financial results, with an operating income of 5.1 billion USD and a net profit of 1.6 billion USD, the highest in the company's history. Richard Forson, President and CEO of Cargolux, praised the Air Silk Road for establishing solid commercial links between China and Europe and said it is critical for logistics and trade (China and the BRI in 2021 and beyond, 2021).

Recent advancements have further optimized this route's efficiency and sustainability. For instance, Shenoyujia (2023) highlights that the Zhengzhou-Luxembourg Air Silk Road has introduced digitalization tools for customs clearance and adopted advanced inspection modes for high-value goods at Zhengzhou Airport. The air corridor has become more efficient, and Zhengzhou has become a significant transport hub. This has boosted trade between China and Europe.

Sustainability is a crucial topic, and these efforts are integrated in the Zhengzhou-Luxembourg Air Silk Road. A cargo flight between Zhengzhou and Luxembourg in June 2023 reduced carbon dioxide emissions using sustainable aviation fuel. This is only part of HNCA's and Cargolux's efforts to make the transition to a more sustainable future low-carbon economy and green aviation fuels, in line with domestic and international goals to reduce by half the global aviation sector's carbon emissions by 2050 (Shenoyujia, 2023).

### **2.5.6 Legal Framework, Risks and the Luxembourg Protocol**

As the BRI grows, dealing with the legal and financial hurdles becomes critical to success and sustainability. China's Belt and Road Initiative, also known as "One Belt, One Road,"

is a massive project to create new rail links to Europe and Southeast Asia. This raises questions about the legal and security issues of rolling stock<sup>15</sup>, as they cross borders, according to Rosen (2017).

This will recreate the old Silk Route, a modern land bridge between East Asia and Western Europe, a faster and more reliable alternative to sea freight. The impact on trade between Asia and Western Europe will be huge. Still, as Rosen (2017) says, it raises complex issues for banks, owners of railway equipment, and railway companies regarding asserting ownership and control of rail equipment that crosses multiple borders.

McBride et al. (2023) describe the BRI as massive, covering overland and maritime infrastructure projects to connect China to Europe, Africa, and other parts of Asia. As China's economic and political muscle grows, the initiative will create a network of railways, highways, energy pipelines, and ports. While the Belt and Road Initiative is an opportunity, it is also a risk for participating countries; some see it as a way for China to export its excess industrial capacity and gain geopolitical leverage over debt and inflated countries.

Unlike the aviation industry, there are no global standards for railway equipment laws, national registers, or tracking systems, according to Rosen (2017). This lack of standardization increases costs and puts rail companies at a disadvantage when seeking funding. For the Belt and Road Initiative to succeed, it needs to attract investments while keeping risks and costs low.

Luckily, Rosen (2017) says there is a solution. The author invokes the Luxembourg Protocol to the Cape Town Convention on International Interests in Mobile Equipment. This protocol makes financing rail vehicles easier by setting up an international registry in Luxembourg, allowing lenders'<sup>16</sup> rights to be tracked worldwide at any time. It lets creditors and railway companies monitor trains across borders, with an option to choose

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<sup>15</sup> Rolling stock refers to vehicles that move on a railway system. It encompasses all trains that are not fixed to the track, such as: locomotives, passenger cars, freight cars, high-speed trains (Rosen, 2017).

<sup>16</sup> Lenders or creditors are individuals, a group (public or private), or a financial institution that makes funds available to a person or business with the expectation that the funds will be repaid (Barone, 2023).

the governing law for financing, regardless of the borrower's<sup>17</sup> location or the vehicle's position.

This protocol creates a reliable system for financing trains and rail equipment, offering consistent rules to protect lenders wherever the trains or borrowers are based. Rail owners and operators in Belt and Road countries can trust that their ownership rights will be upheld, while lenders and investors have security over their assets, even if the borrower defaults, goes bankrupt, or faces government actions. To support the Belt and Road Initiative, major investments in infrastructure, facilities, and rail equipment are needed, much of which will rely on borrowed funds (Rosen, 2017).

During a summit in Beijing in May 2017, China's president, Mr. Xi Jinping, pledged a lending capacity of 55 billion USD indicating the commitment of large and small companies to the initiative's success. The Luxembourg Protocol, as per Rosen (2017), will play a crucial role in facilitating the necessary investments in rolling stock at a reduced cost while ensuring that rolling stock becomes a secure and liquid asset, aligning with the initiative's visionary nature.

Wu (2019) offers critical insights into the range of legal and geopolitical risks tied to the BRI's expansion. The author mentions that the BRI often relies on non-binding MoU's rather than formal treaties, which complicates dispute resolution due to a lack of specific investment treaty rights. Many participating countries are lower-income or developing economies with weaker legal infrastructures, increasing the risks of bribery, corruption, and difficulties in claiming assets. Political instability also poses a challenge; some countries have renegotiated or canceled BRI projects over environmental issues, displacement concerns, or domestic opposition.

BRI projects face material deficit and design change-related issues. Terrorist threats to BRI projects in Baluchistan, Pakistan, add more complexity to these projects. Several arbitral institutions, such as the International Chamber of Commerce, and the Hong Kong International Arbitration Center, have developed specific rules and courts to address these risks. China has established two Chinese International Commercial Courts and introduced the first-ever investment arbitration rules through the China International Economic and

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<sup>17</sup> A borrower is a person or business that receives money from a lender with the agreement to pay it back within a specified period (Bankinter, n.d.).

Trade Arbitration Commission to provide a more robust mechanism for BRI-related disputes (Wu, 2019).

One key issue is that international dispute rulings must be recognized and enforced across borders. Many Belt and Road Initiative countries are not part of the New York Convention, making it difficult. Another problem is sovereign immunity, where states and State-Owned Enterprises (SOEs) can claim they are immune from lawsuits or do not have to pay court-ordered damages. China has softened its stance on SOE immunity, except when SOEs act on behalf of the government. However, foreign investors in China may still struggle with broad interpretations of immunity in Chinese courts, especially concerning foreign SOEs. Thus, investors should carefully examine the legal and political environment of any target country as part of their BRI planning (Wu, 2019).

## **CHAPTER III – SINO-LUXEMBOURG FINANCIAL RELATIONS**

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### 3 Luxembourg as a European Gateway for Chinese Banks

Since establishing relations, Luxembourg and China have had strong links in various sectors such as trade, finance, higher education, tourism, and culture, mentioned in previous chapters (Luxembourg Trade & Invest, 2020).

China's foreign policy vis-à-vis Europe consists of expansion in foreign direct investments, including strategic purchases of firms, implementing the "One Belt, One Road" infrastructure program to link China with Europe, and the internationalization of its currency, the renminbi. Luxembourg, a strategic node in the financial industry, is a perfect hub for China's foreign economic activities. It is the leading European domicile of the RMB Qualified Foreign Institutional Investor scheme, listing Chinese bonds and domicile to critical Chinese investment funds. From this perspective, China views Luxembourg as a gateway to the European markets, especially the European Union: "As a result, it is widely considered the gateway to the EU for Chinese financial institutions." (Funds Europe, 2021).

Luxembourg has become a significant gateway for Chinese firms seeking access to the EU. Seven central Chinese banks, such as the Bank of China, China Merchants Bank, China Everbright, Agricultural Bank of China, Industrial and Commercial Bank of China, Bank of Communications and China Construction Bank, have focused on the country (LFF, n.d.-a). Besides, Chinese investors own shares<sup>18</sup> in two other banks, BIL and Hauck & Aufhäuser. These banks provide services like trade finance, corporate banking, company loans, asset management, and finance investing.

These are banks based in Luxembourg that target Chinese customers who are willing to invest in Europe or European customers who need financing for their activities in China. As LFF (n.d.-b) further explains, the banks have served well as a bridge between Europe and China, creating room for financial deals and promoting economic partnerships between these two continents. According to this source, some characteristics of Chinese banking systems transferred into the local financial sector in Luxembourg. It is worth pointing out that when cultural programs are used to introduce Chinese culture into the investment sector in Luxembourg, its impact can be seen in various business cultures and

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<sup>18</sup> A share represents ownership in a company, typically indicated by a stock certificate. When Chinese banks hold shares in other banks, they become shareholders in those institutions, giving them a stake in the ownership and potential influence over their operations (The Economic Times, 2019).

social life. These banks offer jobs for people wishing to work there, including paid or voluntary internships whereby individuals from around the globe can apply for and exchange foreign ideas while working.

In addition to what has been said thus far, recent developments, including the 2024 China-EU High-Level Economic and Trade Dialogue, have underscored the importance of expanding cross-border RMB transactions and green financing partnerships, further enhancing Luxembourg's strategic role as a bridge between the two economies (Chen, 2024).

Chen (2024) reflects on these developments, noting that “the RMB’s journey from a national currency to one of the world's leading currencies for trade, investment, and reserves reflects our shared commitment to fostering a more diversified and resilient global financial system.” At a recent seminar in Luxembourg, Xu Chen, quoted by Chen (2024), Chairman of the Bank of China Europe SA, emphasized how RMB internationalization offers “a more direct, cost-effective, and efficient means of conducting trade and investment activities, reducing dependency on third-party currencies and enhancing financial efficiency.”

### **3.1 Luxembourg and Hong Kong: A Bridge for Chinese Investment in Europe**

According to Ernest and Young (2017), Chinese asset managers do not invest directly in Europe. They use a so-called “stepping-stone approach,” meaning they set up an intermediary company in Hong Kong, and this intermediary can set up or invest in affiliates in Europe. This way, they can work like an international asset manager. That is also because Chinese people or companies are not allowed to freely invest outside of China without government authorization, according to the regulations there. So, this is the way that these asset managers invest in Europe.

Scholars have argued that Hong Kong is necessary to maintain such leadership for the Greater China capital markets, especially in the long run (Wang et al., 2012). Such leadership predates Hong Kong's role as the world's leading international financial center and gateway to China (Arner et al., 2014). However, with the rapid development of the Shanghai and Shenzhen Stock Exchanges, Hong Kong's leadership position has been increasingly challenged. Scholars have thus called for China to make progress by

attracting more qualified institutional investors worldwide into Chinese investments and doing more to send Chinese investments abroad.

In contrast, Ernest and Young (2017) highlight the Luxembourg-Hong Kong Double Taxation Treaty, established in 2007, as a key agreement for fostering European investments, particularly for Chinese businesses. The treaty aims to eliminate double taxation of income for individuals and companies operating between Luxembourg and Hong Kong. It reduces tax rates and is considered one of the most flexible treaties, especially beneficial for Chinese interests in these low-tax jurisdictions, from both a profit and cash return standpoint.

Further strengthening this relationship, the Memorandum of Regulatory Cooperation on Mainland-Hong Kong Mutual Recognition of Funds (MRF) was signed on 22 May 2015 by the Securities and Futures Commission of Hong Kong and the China Securities Regulatory Commission (CSRC). Ernest and Young (2017) consider it a positive sign. The memorandum permits funds from mainland China to be sold in Hong Kong and vice-versa under a simplified, albeit still somewhat long, process. Likewise, the successful launch of the Shanghai-Hong Kong Stock Connect (StockConnect) in November 2014 is another huge step forward. Like the previous one, this one was taken under the MRF.

These initiatives provide significant investment opportunities for Chinese and Hong Kong investors and offer unprecedented access to capital markets. The MRF is seen as setting a new international standard for fund regulation in Asian financial markets, with Ernest and Young (2017) describing it as "the first of many to come" and expecting its expansion throughout the region.

In this context, the Luxembourg-Hong Kong link serves as both an economic entryway for China into Europe and a means of cultural exchange. It promotes mutual understanding of business practices in Europe and Asia, bridging the gap between European and Asian cultures in the realm of business.

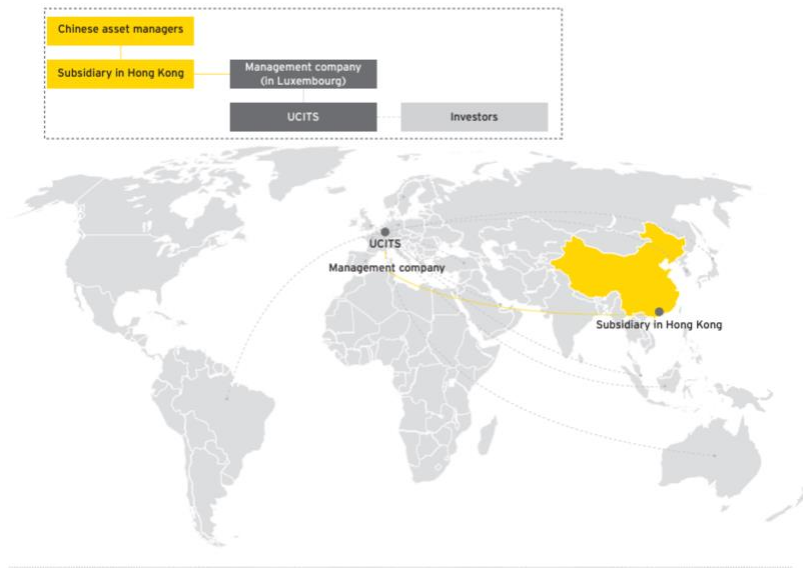


Figure 8 – Example of asset managers using Luxembourg UCITS. Source: Ernest and Young (2017).

### 3.2 The QFII and RQFII Impact

The Qualified Foreign Institutional Investor (QFII) program, initiated in 2002, was China's major push into internationalizing its mainland financial markets. It allows foreign investors to access a wide range of products within China's diverse and complex markets using foreign currencies, such as EUR and USD. Often described as one of the few programs that survive due to their efficacy and efficiency, QFII epitomizes the positive changes in international investment for both sides of the yuan border (Wang & Xu, 2024).

Following the success of QFII, in December 2011, China launched the RQFII program. Initially, this program only allowed Chinese financial institutions to create renminbi-denominated funds in Hong Kong. However, RQFII later expanded to various other jurisdictions, giving them allowances between 50 and 80 billion yuan, specifically Luxembourg, United Kingdom, Singapore, France, Korea, Germany, and Canada, according to The Globe and Mail (2015). This move helped push China's financial integration with the rest of the world and the renminbi's internationalization as a currency investment tool.

Tan (2014) observes that the RQFII program has eased operations considerably and has not been overtaken by the QFII program. For Tan (2014), the critical change from the

QFII program to the RQFII program is that the latter permits direct investment using external RMB and upgrades the vision of the QFII program to an expanded investment scope. He values the CSRC opening of the onshore bond market to the RQFII program. He welcomes private equity funds to be included among the investments that can be made using RQFII quotas. Moreover, the author notes that the RQFII program's success will support China's push for broader renminbi adoption as a key international currency.

These schemes provide Luxembourg with direct access to the Chinese financial markets. Hence, funds based in Luxembourg can establish a better foothold in the Asian markets. This access to Chinese markets helps Luxembourg and the funds establish their Asian presence. Luxembourg is taking advantage of these opportunities to access the Chinese market and strengthen its position as the financial gateway between Europe and Asia. The evolving QFII and RQFII rules, as per the Shanghai Stock Exchange (n.d.), make these schemes attractive to investors looking to diversify into China, which fits with Luxembourg's strategy to be the bridge between European investors and Asian markets.

### **3.2.1 Key reform**

As the QFII and RQFII programs gained influence, China implemented further reforms to support increased accessibility and investor engagement. In 2019, China eliminated the total investment limits for QFII and RQFII schemes, enhancing the flexibility available to foreign investors (Wang & Xu, 2024). UBS Asset Management (n.d.) highlights that investors must still go through a reporting procedure with the State Administration of Foreign Exchange. This procedural requirement indicates that even though strict investment restrictions are not being enforced anymore, some regulatory monitoring is still necessary for maintaining supervision. China's cautious approach to financial liberalization maintains a balance between flexibility and oversight by providing increased market access with the implementation of necessary regulatory mechanisms.

In recent news, Tong and Zhang (2024) state that in July 2024, a significant reform merged the QFII and RQFII regimes, relaxed requirements, reduced paperwork, shortened the review time, and made the overall process simpler. According to the Shanghai Stock Exchange (n.d.), the merger removed the limit on the number of intermediaries that can assist QFII or RQFII investors, improved supervision over reporting and filing, and reduced data submission. This has made QFII and RQFII more open and efficient for international investors.

### **3.3 Luxembourg's Role to Expand RMB**

The renminbi is going global, and financial centers around the world are competing to capture a slice of this growing market. While Hong Kong remains the clear leader in the offshore RMB hub race, Luxembourg has solidified its position as the primary RMB hub within the Eurozone. According to The Business Report (n.d.), Luxembourg is the number one destination in the Eurozone for RMB-denominated financial services, and its influence continues to grow, particularly in light of the United Kingdom's exit from the European Union.

While it may seem surprising that China, with a population of 1.4 billion, has taken a keen interest in Luxembourg, a country with just over half a million residents, this reflects the strategic importance of the Grand Duchy in China's global financial ambitions. Luxembourg has emerged as a key player in the internationalization of the renminbi since Beijing designated it as one of the few global trading hubs for RMB. As a result, Luxembourg now plays a significant role in RMB investment fund administration, the listing of Dim Sum bonds, and facilitating Chinese investment flows into Europe (The Globe and Mail, 2015).

Chinese investors have found Luxembourg to be an attractive destination due to its flexible and innovative financial infrastructure. According to Center (2022), Luxembourg's fund industry offers a broad range of investment products across various asset classes, particularly appealing to Asian investors. Its reputation as a center of excellence in cross-border fund administration and structuring makes it a natural choice for investors seeking to expand their European presence. Luxembourg's multilingual workforce, political and economic stability, and strong regulatory environment further enhance its appeal, as mentioned previously.

As the Tianjin Commission of Commerce (n.d.) says with the United Kingdom leaving the EU, the Grand Duchy, the second financial center after London, is seeing more and more Chinese financial institutions setting up and opening branches. We should not overstate the impact of Brexit, but many Chinese banks have found Luxembourg to be an alternative gateway to the European Union's single market. Tianjin Commission of Commerce (n.d.) adds that Luxembourg has also become a significant hub for the internationalization of the RMB with 50 billion yuan of RQFII and will further promote

the use of the renminbi in trade and investment in Luxembourg. Luxembourg is the destination for investment funds from China.

Luxembourg's role in the RMB market extends beyond fund administration. The country is a major issuer of RMB-denominated financial products, including deposits, loans, bonds, and mutual fund assets. According to Yang, quoted by *The Globe and Mail* (2015), the Chinese government wants long-term investors in the domestic market. The RQFII scheme has played a vital role in developing the international RMB investment fund market and allows overseas investors to use offshore renminbi deposits to invest in mainland tradable holdings. Asset managers in some countries have struggled to use their investment allowances, but not in the small country of Luxembourg.

In 2016, 65% of all European funds investing in China were based in Luxembourg (Segal, 2021). That number has increased to 72.1%, as seen prior by LFF (n.d.-a) quoting PwC & Lipper (2024). Commission de Surveillance du Secteur Financier (CSSF), Luxembourg's financial regulator, has been instrumental in allowing European funds to access the Chinese domestic bond market and the A-share market<sup>19</sup> (Tianjin Commission of Commerce, n.d.). This has strengthened Luxembourg's position as a gateway for European investors seeking exposure to the Chinese market.

According to the Tianjin Commission of Commerce (n.d.) based on the UN Conference on Trade and Development, in 2016, funds domiciled in Luxembourg invested a substantial amount of 1.42 trillion EUR in euro-area corporations and governments. There were 358 billion EUR invested in other EU member states, showcasing Luxembourg's significant contribution to the investment flows within the European Union.

Luxembourg has become the number one destination for international funds investing in China, ahead of Hong Kong and the USA. 37.6% of global funds investing in China are based in Luxembourg, so it is the go-to destination for fund managers. Many big names in the industry, such as Aberdeen, BlackRock, Fidelity, First State, HSBC, JP Morgan, Schroders, and Deutsche Bank, have chosen Luxembourg as the domicile for their RMB funds. Chinese asset managers have also chosen Luxembourg as the location for their European funds launched through their Hong Kong affiliated entities (LFF, n.d.-b).

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<sup>19</sup> China A-shares are the securities of Chinese companies listed on the two Chinese stock exchanges, Shanghai and Shenzhen (Segal, 2021).

The Business Report (n.d.) adds that almost half of Chinese foreign direct investment into the Eurozone goes through Luxembourg. The Grand Duchy is the world's number one in cross-border investment funds, and that expertise has attracted renminbi fund promoters.

The Luxembourg Stock Exchange plays a central role in RMB internationalization. As the primary market outside of Asia for RMB-denominated Dim Sum bonds, LuxSE has listed over 60 bonds with a combined value of 35 billion yuan. This solidifies Luxembourg's reputation as a global hub for RMB-denominated securities, providing a seal of approval for the high standards and security offered by the LuxSE (LFF, n.d.-b).

Luxembourg's success in attracting RMB investments can be largely attributed to its flexible legal and regulatory framework. The country offers a range of investment structures, such as Société d'Investissement à Capital Variable (SICAV) and Specialized Investment Funds (SIF), which comply with both UCITS (Undertakings for Collective Investment in Transferable Securities) and AIFMD (Alternative Investment Fund Managers Directive) frameworks. These structures are widely recognized across Europe and globally, making Luxembourg an attractive jurisdiction for RMB fund promoters and investors (LFF, n.d.-a).

Luxembourg's strong financial services sector and expertise in cross-border fund administration have positioned it as a "problem solver" in international finance, particularly through its participation in the UCITS framework. This regulatory framework, developed by the European Commission, allows investment products to be marketed across the European Union, enabling Luxembourg to become the leading European center for RMB funds. By the end of 2014, Luxembourg was responsible for managing RMB-denominated assets totaling 296 billion yuan in domiciled funds, making it the second-largest fund domicile in the world (Chen, 2019). Nowadays, over 300 billion yuan in RMB-denominated assets are based in Luxembourg, making the Grand Duchy the largest RMB hub among EU countries (The Business Report, n.d.).

In addition to these regulatory advantages, Luxembourg's network of double taxation treaties helps reduce the tax burden on global investments, further enhancing its appeal to Chinese investors. The country's financial regulator, CSSF, is known for its accessibility and efficiency, offering tax benefits and a strong regulatory framework that promotes the growth of RMB fund management. This has made Luxembourg a key facilitator in the RMB's global expansion, particularly in Europe, where it serves as the

leading hub for Chinese institutions conducting cross-border business (The Globe and Mail, 2015).

### **3.4 Luxembourg UCITS and Strategic Relationship with China**

An essential and developing part of the global financial structure is UCITS in Luxembourg and its existence in China. The relationship between these two countries concerning UCITS is of particular interest. As will be made clear in the following subsections, using the UCITS structure facilitates the reduction of investment risk for investors by making fund operations more transparent.

As stated, the UCITS Directive is a European Commission's framework that allows investments to be marketed throughout the European Union and the rest of the world. Before UCITS, investing outside each country's borders was complicated; each state had its tax laws. So, the approval of this directive opened the market and democratized access for investors, especially private investors, to invest in investment funds. According to Kozłowska-Sugar (2016), UCITS accounts for 75% of all collective investments by small European investors. This directive also gave consumers more protection.

Kozłowska-Sugar (2016) adds that UCITS give EU investors safe and easy access to savings in shares, bonds, and other similar financial instruments from around the world. These assets are not held by the fund itself but by separate specialized companies (usually banks) called depositaries. Depositaries must control and protect these assets even if they are kept in non-EU bank accounts. Depositaries also must make sure fund managers comply with all relevant rules.

#### **3.4.1 Luxembourg's Position in the Global Financial Market**

Including RQFII investment allowances in the UCITS framework has boosted Luxembourg's global footprint. UCITS funds domiciled in Luxembourg can now use RQFII quotas to invest directly in China, offering investors China exposure. Recent changes to the QFII scheme have made it even more attractive for Luxembourg-domiciled UCITS funds. The 100% total asset access in China means these funds can fully tap into China's growth. This is another proof of Luxembourg's status as a leading fund domicile and its ability to be a gateway for foreign investments into China (Elvinger Hoss, 2018).

The combination of QFII and RQFII regimes allows Luxembourg UCITS funds to access a broader range of Chinese financial products, including equities, bonds, and other

financial assets. This is another step in Luxembourg's development as a central RMB hub and gives global investors access to the Chinese market. Arendt & Medernach, a leading independent business law firm in Luxembourg, has contributed to this new access channel, highlighting Luxembourg's ability to adapt to regulatory changes and maintain UCITS compliance (Arendt, 2016). This regulatory flexibility makes Luxembourg an even more attractive domicile for international funds, with efficient and compliant access to China.

### **3.4.2 Case Study: Bank of China (Luxembourg) SA and CACEIS Collaboration**

To emphasize the RQFII scheme, the Bank of China (Luxembourg) SA and CACEIS<sup>20</sup> have used it to increase investment opportunities and operational efficiency. The Bank of China (Luxembourg) SA, a subsidiary of one of China's biggest state-owned commercial banks, has been vital to the internationalization of the RMB and the expansion of Chinese financial services in Europe. In April 2015, Luxembourg received a 50 billion RMB RQFII quota, making it a leading European center for RMB investments (Arendt, 2015).

CACEIS, a major European asset servicing company, provides custody, depositary, fund administration, and distribution services. With its solid resources and know-how, CACEIS is the ideal partner for the Bank of China (Luxembourg) SA to manage the RMB RQFII UCITS fund. The partnership employed the RQFII quota to strengthen Luxembourg's status as an RMB hub. This involves using the quota to permit direct investment in the onshore Chinese marketplace and to give global investors access to all kinds of Chinese assets, such as stocks<sup>21</sup>, bonds, and mutual funds<sup>22</sup>.

The partnership, as mentioned by Crédit Agricole (2015), followed a structured approach: Bank of China (Luxembourg) SA obtained the RQFII license and quota from the Chinese authority (CSRC) while CACEIS ensured compliance with the Luxembourg regulatory requirements, coordinated with the CSSF to launch the RMB RQFII UCITS fund. The fund was UCITS compliant, known for its rigorous regulatory and investor protection, and complied with Chinese and Luxembourgish regulations. CACEIS integrated its

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<sup>20</sup> CACEIS is a bank partnership of Crédit Agricole and Santander.

<sup>21</sup> A stock is a general term used to describe the ownership certificates of any company (The Economic Times, 2019).

<sup>22</sup> A mutual fund is an investment fund that combines money from many investors to purchase securities, such as stocks or bonds (U.S. Securities and Exchange Commission, 2022).

services to support the RMB RQFII UCITS fund, increase operational efficiency, and reduce administrative burdens.

The result was astonishing. Crédit Agricole (2015) points out that using the fund gave investors direct access to China's onshore markets, letting them diversify their portfolios by selecting high-quality Chinese assets. CACEIS services were integrated into the fund, allowing them to pivot toward investment strategy and compliance at the speed of thought. Moreover, the investors' confidence in this fund was enhanced by what Crédit Agricole (2015) describes as "Luxembourg's solid regulatory framework," which has authorized the fund, and by the strategic use of the RQFII quota to augment the investor's selection of RMB assets.

Even with success, the partnership faced hardships: navigating through intricate regulatory setups and unpredictable market risk. Both partners overcome these challenges by opening conversations with regulators and efficient risk management. For CACEIS, especially, this put their experience and skill set to the test. More than ever, integrating services seamlessly across borders requires CACEIS's ability to coordinate finely on many levels, with meticulous attention to detail.

The collaborative relationship between the Bank of China (Luxembourg) SA and CACEIS will continue to improve. Profitable developments in investment products such as exchange-traded funds and private equity will herald another technological development in which digital technology is more efficient. Investors are where capital is, and Luxembourg will continue to be a hub for that, thanks to its infrastructural development and diversified portfolio solutions.

### **3.4.3 Access to Chinese Market**

Luxembourg UCITS can now access the Chinese market directly through the StockConnect schemes. This allows UCITS funds to invest in shares listed on the Shanghai and Shenzhen Stock Exchanges via the Hong Kong Stock Exchange. This is a big plus for Luxembourg-based UCITS to tap into the Chinese equity markets. As Juncker (2017) said, there are no limits for asset managers in the StockConnect framework, and so far, there has not been a problem. Luxembourg is the leader in UCITS through this channel.

Chinese bonds are also a focus of attention. Interest is really at a basic level with bonds right now. Since 2016, the People's Bank of China has allowed direct access to the China Interbank Bond Market for foreign investors. BondConnect, in effect, allows direct trading with the domestic bond market for foreign investors (Juncker, 2017). Once you have set up an account within Hong Kong's international finance center, you can trade with the mainland and buy and hold local bonds via BondConnect.

As Juncker (2017) said, these funds are mainly structured under the UCITS framework and are designed to give international investors access to the Chinese market. The selling points are the local expertise and presence of these asset managers and banks in the Chinese market. These platforms will be able to give Chinese investors access to international capital markets as China's capital controls are gradually relaxed (Association of Luxembourg Fund Industry, 2014).

In the broader context of foreign investment in China, Juncker (2017) says that it is subject to strict limitations and can only go through specific channels approved by the Chinese government. For UCITS, accessing the Chinese market is critical. This can be done in several ways, including the quota system, direct access via the StockConnect programs, and direct access to the Chinese bond market requiring Hong Kong help as an intermediary.

Interestingly, even before Luxembourg obtained its own RQFII quota, Luxembourg funds had access to this investment channel. The Chinese authorities had permitted Luxembourg UCITS to utilize the RQFII quotas of the countries where their external managers were based. For instance, if a Luxembourg fund appointed a manager based in Hong Kong, that manager could utilize the Hong Kong RQFII permitted allowance on behalf of the Luxembourg fund. Following the granting of Luxembourg's own RQFII quota in 2015, Luxembourg management companies (Verwaltungsgesellschaften) are now able to outsource the management of UCITS funds using their RQFII quotas to investment managers who do not possess their own RQFII quota (Juncker, 2017).

Simply put, China is very interested in Luxembourg, and the connection is mutual. Figure 9 better depicts this.

Luxembourg is a natural gateway for investment flows in and out of China.

- Luxembourg is recognized as the global hub for cross-border investment funds offering Chinese asset managers a platform to launch an investment fund product and to distribute it on a cross-border basis – i.e., not only in Europe but back to Asia and across the globe.
- The MoU signed between the Luxembourg and Chinese regulators makes Luxembourg one of the few financial centers to have such an agreement, enabling QDIIIs to invest directly in Luxembourg-regulated financial products, including investment funds domiciled in Luxembourg.
- Luxembourg is actively building relationships with China and other Asian countries and has concluded 14 double taxation treaties with various Asian countries or regions (including the People's Republic of China, India, Indonesia, Japan, Laos, Malaysia, Mongolia, Thailand, Sri Lanka, Singapore, South Korea, Vietnam, Taiwan and the Hong Kong Special Administrative Region).
- Today, Luxembourg is the most important hub for cross-border RMB business in the Eurozone. Luxembourg ranks first in Europe when it comes to RMB deposits (61.5 billion RMB), loans (61.1 billion RMB) and RMB in investment funds (296.3 billion). The Luxembourg Stock Exchange is also the exchange with most Dim Sum bonds listed in Europe (number: 45).<sup>1</sup> The combination of the strengths of Luxembourg as a leading global investment fund hub and RMB-related business development could offer huge opportunities to fund managers.

Luxembourg offers investors:

- A strong tradition of investor protection
- A stable democracy and strong economy: Luxembourg is a founding member of the European Union
- A knowledgeable and responsive regulator
- Proactive legislation: a close working relationship between the business community, the government and legislators that underpins Luxembourg's innovative legal framework
- A tradition of financial expertise
- A unique concentration of investment fund industry professionals in all aspects of product development, administration and distribution
- Extensive experience in technical investment fund solutions, including multiple share classes and pooling
- Service providers such as depositories, custodians, fund administrators, fund lawyers, audit firms and tax advisors experienced in cross-border registration of both UCITS and alternative funds



Figure 9 – Luxembourg as a natural gateway for Chinese investment. Source: Ernest and Young (2017).

### 3.5 Other Investment Funds

While UCITS are designed for private investors with high levels of investor protection, other investment schemes such as real estate, private equity, venture capital, and hedge funds are outside the UCITS Directive. These are governed by the AIFMD which aims to enhance investor protection and transparency of fund operations, as Ernest and Young (2017) say.

Non-UCITS funds classified as Alternative Investment Funds (AIFs) under AIFMD have a different regulatory and distribution landscape. The distribution of AIFs in Europe largely depends on where the fund and its managers are based. European-based AIFs managed by European entities have an approved European marketing passport and can be distributed more easily across borders. Non-European AIFs or those managed by non-European entities are subject to the specific distribution rules of each country they target.

Ernest and Young (2017) say this may change as the EU considers extending the marketing passport to non-European managers and funds depending on their jurisdiction.

The AIFMD regime is designed to create a global brand for non-UCITS funds. Ernest and Young (2017) say Luxembourg, with its experience in managing and distributing UCITS products, is well-positioned to replicate this success for alternative funds and leverage its reputation and expertise as a financial center.

In Luxembourg, according to Ernest and Young (2017), the standard vehicles for AIF are:

- Specialized Investment Fund: Flexible regarding investment policy and eligible investors, suitable for various alternative investments.
- Investment Company in Risk Capital: Focuses on risk capital investment in innovative or growth companies.
- Financial Holding Companies: These are mainly used for structuring investments and are often combined with SIF or companies in risk capital. They can be set up as shared funds, investment companies, limited liability companies, or partners tax transparent or opaque.

Peter and Rao (2024) mention that specific legal entities play a crucial role in Chinese investments in Luxembourg. The most common structures used by Chinese investors are private limited liability companies (*Société à Responsabilité Limitée*, SARL) and public limited liability companies (*Société Anonyme*, SA), with SARLs often preferred due to their lower capital requirements.

For fund investments, Chinese investors often use the reserved alternative investment fund, which do not require CSSF supervision, and the SIF as limited partnerships. Another popular entity is the investment company in risk capital (*Société d'Investissement en Capital à Risque*, SICAR) for pooling capital<sup>23</sup> for various investments (Peter & Rao, 2024).

According to Peter and Rao (2024), these entities must have a substantial presence in Luxembourg, including minimum share capital and local management. This means that critical decisions are made in Luxembourg to comply with the country's regulations to protect investors and maintain financial soundness.

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<sup>23</sup> Pooling capital refers to the aggregation of funds from multiple individual investors to create a single or larger investment portfolio (Chen, 2020).

### 3.6 Fintech Investments

Kagan (2024) defines fintech as a new technology that improves and automates the delivery and use of financial services. At its core, fintech helps companies, business owners, and consumers manage their finances, processes, and lives. Its software and algorithms run on computers and smartphones. Fintech is short for “financial technology.”

When fintech emerged in the 21st century, the term was applied to the technology behind the scenes of established financial institutions like banks. From 2018 or so to 2022, it shifted to consumer-facing services. Fintech now includes education, retail banking, fundraising, and nonprofit and investment management. According to Kagan (2024), fintech also includes cryptocurrencies like Bitcoin.

Kagan (2024) explains that fintech has evolved since 2011, with startups raising billions. The author notes that North America still produces most of the fintech startups, Asia is second, and Europe is third. Some of the most active areas of fintech include:

- Cryptocurrency (Bitcoin, Ethereum, etc.), digital tokens (non-fungible tokens), and digital cash.
- Regtech helps financial service firms meet industry compliance rules, especially regarding Anti-Money Laundering and Know-your-customer protocols that fight fraud.
- Robo-advisors like Betterment use algorithms to automate investment advice to lower costs and increase accessibility.
- Cybersecurity. With the rise of cybercrime and decentralized data storage, cybersecurity and fintech are intertwined.
- Unbanked/underbanked services refer to financial solutions aimed at disadvantaged or low-income individuals who are either excluded or inadequately served by conventional banking institutions or mainstream financial services providers.
- AI chatbots, which became popular in 2022, are another example of a fintech in our daily lives.

Dettoni (2019) says Luxembourg is moving forward with China, especially in fintech and Green Finance. Despite being the second smallest EU member, the Grand Duchy is making a name for itself in the emerging parts of the financial industry.

In fintech, Dettoni (2019) says that Brexit has reinforced Luxembourg's position as a go-to destination for global payment and e-commerce companies. Companies like PayPal, Amazon, and Rakuten have chosen Luxembourg as their base.

Chinese e-payment solution provider, PingPong was the first Chinese fintech company to invest in Luxembourg in 2017. In 2018, PingPong further deepened its presence by announcing a 100 million EUR investment plan, which included R&D. PingPong, supports Chinese e-commerce merchandisers with electronic payments and has acquired a payment institution license in Luxembourg (Mironescu, 2017). Alibaba's e-payment company, Alipay, also set up shop in Luxembourg to mitigate the risks of Brexit and to be able to do business in the EU.

China's technology giants are coming to Luxembourg. TikTok and its parent company ByteDance have moved their focus to Luxembourg after a failed attempt in Ireland. ByteDance is now looking to get an e-payment license in Luxembourg and is further establishing itself in Europe. The company signed a contract with The Office, a coworking space that hosts Spotify and Wolt. TikTok's interest in Luxembourg fits with the company's plans to develop its payment system and expand in Europe after running into regulatory issues in other countries (Labro, 2024). ByteDance's move shows Luxembourg is becoming a digital finance hub not only for payment solution providers but also for bigger tech companies looking to integrate fintech into their platforms.

Despite its small size, Luxembourg has established a significant presence in Chinese finance, as we can see. As China continues to develop its financial markets and fintech industry, Luxembourg is poised to reap the benefits of this growth. However, integrating technology in financial services is a double-edged sword for Luxembourg because keeping up with China's pace is critical to staying competitive.

### **3.7 Green Finance and International Development**

European Commission (2024) defines green finance as considering Environmental, Social, and Governance (ESG) in business and investment decisions beyond financials.

Sustainable finance is the chance to move financial flows into investments that help the world achieve a low-carbon, sustainable, and fair economy.

Several initiatives have been set up internationally and in Luxembourg to build resilient and carbon-neutral economies. The Luxembourg Government and The Ministry of Finance have a specific role and responsibility in sustainable finance initiatives, negotiating, implementing EU legislation, setting policy, creating national initiatives, and participating in international initiatives to accelerate and maintain sustainable finance. In sustainable finance, the Ministry of Finance has a dedicated team and is a board member of four local and six national committees. The Ministry also represents Luxembourg in three international organizations and three European level working groups and supports four international initiatives (The Luxembourg Government, 2024).

Luxembourg has a long history of supporting Chinese corporate banking in Europe, international asset management, and access to Chinese capital markets. Dettoni (2019) says the country's commitment to green finance is evident in its second position in the Global Finance Index.

Luxembourg's application to become a founding member of the AIIB was approved in 2015, and the Grand Duchy is the first non-regional founding member of the AIIB. Luxembourg wants to attract more green bonds<sup>24</sup> from Chinese issuers, including the AIIB, which launched a 500 million USD sustainable bond program in July 2019 (Danny Alexander, n.d.).

One area with significant growth potential is ESG and green investments. Patel (2021) highlights the creation of the Green Bond Channel in 2018, a collaboration between the LuxSE and the Shanghai Stock Exchange. This initiative allows investors to access information in English about Chinese domestic green bonds listed in Shanghai, laying the foundation for further developments. Chris Hollifield, head of the China desk at Luxembourg for Finance, emphasizes the importance of green finance in both Europe and China. This focus is reflected in European Commission President Ursula von der Leyen's Green Deal and Chinese President Xi Jinping's commitment to peak emissions by 2030 and achieve carbon neutrality by 2060.

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<sup>24</sup> Green bonds are a type of investment used to finance projects that benefit the environment. They support sustainable and eco-friendly initiatives, helping to address climate change and promote a greener future (Iberdrola, n.d.).

Funds Europe (2021) says Luxembourg's expertise in asset management, especially in China, and its early mover advantage in green finance makes it a hub for investment flows between international investors and green projects in China. However, as investors want to access China more, the differences in market standards, including the definition of green products, must be addressed.

ESG and green investment will be a big topic and an ample opportunity in the future, as Peter and Rao (2022) reflect. The Chinese government has been increasingly encouraging sustainable investment practices and prioritizing ESG factors in overseas investment since the "Belt and Road Initiative" was incorporated into the Constitution of China in 2017. Chinese investors must consider ESG standards when evaluating outbound investment opportunities in Luxembourg and the EU.

China's commitment to carbon neutrality shows there is room for many green products. Luxembourg can also help to align China's taxonomy for sustainable investing with European standards. Given China's increasing internationalization and geopolitics, the timing of these developments is unclear.

### **3.8 Current or Possible Challenges**

From a political and economic perspective, Luxembourg and China are worlds apart. The geopolitical landscape, especially the tensions between China and the United States of America, impacts Luxembourg through its financial ties with China. Luxembourg must maintain its financial relationship with China while respecting EU and international rules. A strategy that balances economic interests with diplomacy will be vital to keeping Luxembourg as a financial bridge between China and Europe in the ever-changing geopolitical landscape.

However, Meyer (2023b) mentions the meeting with Vice Prime Minister Xavier Bettel and Chinese President Xi Jinping. In that meeting, the Luxembourgish Vice Prime Minister said: "We will have good bilateral relations with China, as long as it is in our economic interest and our values, including human rights."

The Association of the Luxembourg Fund Industry quoted in Meyer (2023b), still in the interview context, took its approach by stating that it is crucial to maintain dialogue, commercial relations, and economic relations but also consider the geopolitical tensions that are key in the international sphere. The outgoing director of the association, Camille

Thommes, added: “Luxembourg was a pioneer in opening up access for global investors to Chinese financial products and allowing UCITS funds to be exposed to such products. However, while the channels are open, we do not decide whether it is in the interest of investors, institutional or private, to be exposed to China or not.”

Gordon (2023) emphasizes that despite the geopolitical tensions and China’s recent economic difficulties, Luxembourg’s former finance minister, Yuriko Backes, engaged in fruitful dialogues during a recent delegation to China, underscoring the strength of Luxembourg’s bilateral relations and its commitment to embedding sustainable finance. These dialogues included significant discussions with Yi Huiman, President of the China Securities Regulatory Commission, focusing on the opening and internationalization of the Chinese capital markets and asset management.

Gordon (2023) quotes Nicolas Mackel, CEO of Luxembourg for Finance, who highlighted the critical nature of these engagements: “The core of our relationship is that Luxembourg investment funds are leading the world in channeling capital from global investors into Chinese A-shares and bonds. This relationship, contingent on global economic and geopolitical realities, underpins our strategic financial interactions with China.”

Gordon (2023) addressed that the meetings mentioned regulatory challenges, with differences in financial reporting requirements, investor protection laws, and fund management regulations between the EU and China. These discussions are crucial as they impact the operations of Luxembourg-domiciled funds significantly invested in China.

Meyer (2023a) noted that the Chinese economy is facing challenges such as deflationary pressure, a property crisis, fragile trade, and weak demand, leading international investors to avoid its market. This does not benefit Luxembourg as a whole. The nation has established itself as a leading hub in Europe for cross-border yuan transactions and a significant center for investments connecting China and Europe.

Meyer (2023a) reflects that investment funds focused on a Chinese strategy experienced notable withdrawal of capital in 2023. While the numbers may appear small compared to the over 5 trillion EUR in assets managed in the Luxembourg fund sector, the direction is downward. Total assets owned by residents of Luxembourg in China dropped from 126.9 billion EUR to 79.3 billion EUR from June 2021 to June 2023, according to the Luxembourg Central Bank. This signifies a drop of nearly 40% within two years.

Luxembourg’s financial sector is heavily exposed to Chinese investments, and the recent economic strains in China, such as the slowdown and regulatory tightening in various sectors, have introduced significant risks.

As seen in Figure 10, these drops result from a global pattern, mainly caused by economic factors such as low interest rates, poor financial performance, and yuan depreciation in China. Geopolitical reasons, like heightened monitoring of Chinese capital movements in and out of the United States and Europe, also play a role under Meyer (2023a).



Figure 10 – Luxembourg assets in China. Source: Meyer (2023a).

However, interest is still present in yuan-denominated bonds. Figure 11 serves as a source and emphasizes the wording at this moment.

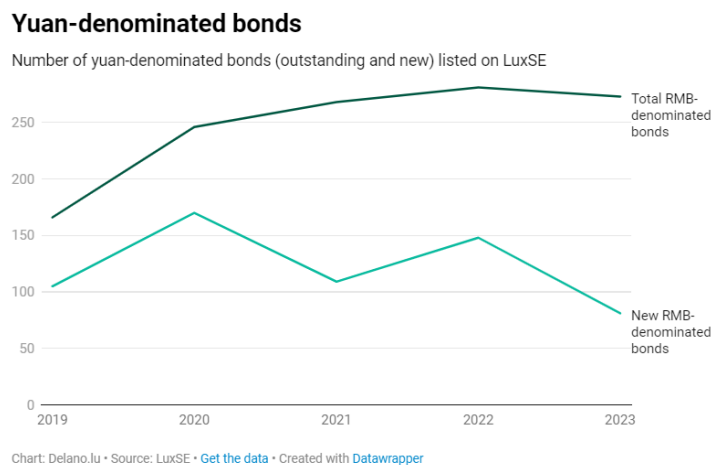


Figure 11 – Yuan-denominated bonds listed on LuxSE. Source: Meyer (2023a).

The trend has kept growing and pushed through the COVID-19 difficult periods. Still, lately, it has seen somewhat of a smaller growth than what was expected, as Meyer (2023a), quoting Nigel Fielding, former CEO of HSBC Luxembourg, emphasizes:

“Investors have been cautious for about a year, and I do not see any change in the short term. However, interest in China is still there. Luxembourg has a solid infrastructure, and the long-term outlook is positive.” This is further evidenced by the signing of a Memorandum of Understanding between the Luxembourg Stock Exchange and China Everbright Bank to promote financial market integration between Europe and China (Gordon, 2023).

The outlook for Chinese investment into Luxembourg is still good, according to Peter and Rao (2022), as the legal and political stability of Luxembourg’s regulatory and legislative framework and the growing fund industry and financial sector are still the key drivers for Chinese investors to make investment decisions even during pandemics. Peter and Rao (2024) argue that the ESG area is becoming more critical in investment decision-making. Chinese investors should, therefore, enhance their competitiveness and grab the opportunities in Luxembourg and the broader EU market by developing ESG expertise and aligning their investments with sustainability goals.

Geopolitics will be the main factor affecting the relations between China and the EU. The impact of the war in Ukraine and geopolitical tensions in the Middle East on China’s investment will depend on the development of the crisis and the stance the Chinese government takes towards the conflicts. However, these tensions have already triggered intense debates on critical infrastructure and resilience in Europe, which could, in turn, increase scrutiny of Chinese investment in several industries, including infrastructure, transport, and energy. Investments focusing on specific sectors, such as consumer goods and infrastructure, will be more attractive to Chinese investors (Peter & Rao, 2024).

## **CONCLUSION**

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This thesis delved into the growing financial ties between China and Luxembourg, showing how this small but strategic European nation has become a crucial entry point for Chinese capital. Luxembourg's shift from a farming focused economy, to respected steel producers, to a global financial powerhouse has made it a key ally for China, especially in projects like the Belt and Road Initiative and the wider use of the renminbi through specific programs, such as QFII, RQFII, UCITS and other investment mechanisms mentioned throughout the work.

Several factors have contributed to Luxembourg's emergence as a major hub for Chinese investment. The country's long history of adapting to economic changes, forward-thinking regulations, and a business-friendly climate have all played significant roles. Luxembourg has become a key player in facilitating Chinese investment in the EU, with financial institutions leveraging programs like RQFII to access Chinese capital markets, as well as utilizing UCITS funds. Additionally, the Luxembourg-Hong Kong Double Taxation Treaty has positioned Luxembourg as a preferred destination for Chinese investment in Europe. Its central location within the European Union further enhances its appeal, providing Chinese investors with easy access to the EU's single market and solidifying Luxembourg's role as a financial gateway.

A key finding of this research is Luxembourg's ability to stay ahead in financial innovation. It is not only attracted traditional financial services but also become a leader in new areas like green finance and fintech. Luxembourg's flexibility has made it an appealing partner for China, as China's global financial strategy now includes a focus on sustainable and tech investments. Luxembourg's role as a hub for renminbi investments has strengthened its part in the global growth of China's currency and financial operations.

Addressing the main research question: "What factors have contributed to Luxembourg's role as a significant financial hub for Chinese investments, and what are the wider implications for both nations?" we can point to five main factors behind Luxembourg's rise as a key financial hub for Chinese investment and China's aspirations in Europe.

First, Luxembourg's history of adapting has been crucial to its success. Over the past 200 years, the country has changed from a rural society to one of the world's top financial centers. This shift began with Luxembourg moving away from a steel-based economy in the 19th and early 20th centuries to becoming a leader in financial services after the steel industry declined.

Regulatory foresight is another important factor behind Luxembourg's success. The country has set up business-friendly rules that make cross-border investing easy while still meeting global standards. Key programs like RQFII and UCITS have helped Chinese firms work smoothly in Europe. Luxembourg has become a top spot for Chinese investments in Europe by offering new financial tools like renminbi funds and Dim Sum bonds. The focus on green finance and fintech has also lured Chinese investors interested in sustainable and tech-driven finance.

Luxembourg's strategic central location in Europe has boosted its status as a financial hub. It gives Chinese investors direct access to the EU's single market of over 500 million consumers. This is crucial for Chinese businesses looking to grow in Europe. Luxembourg's proximity to major financial cities like Frankfurt, Paris, and London, along with its multilingual workforce and strong infrastructure, make it an ideal base for Chinese financial operations.

Luxembourg's ties with China have grown stronger through diplomacy and cultural exchanges, reinforcing their economic partnership. The two countries established formal relations in 1972 and have since strengthened their bond. Luxembourg's involvement in China's Belt and Road Initiative, like its part in the CFL-Chengdu collaboration, Zhengzhou-Luxembourg Air Silk Road, shows its commitment to economic cooperation, global rail trade, air trade. The growing Chinese community in Luxembourg, plus educational and cultural programs like the Confucius Institute at the University of Luxembourg, have improved the understanding between the two nations. These cultural links add depth to the growing financial ties.

This partnership has important wider effects for both countries. Working with China boosts Luxembourg's standing in global finance and strengthens its role in Europe's financial network. Luxembourg's ability to adapt its financial systems to China's needs and focusing on a niche finance ensures its relevancy in global markets. For China, Luxembourg serves as a key gateway to the EU, allowing a smooth flow of Chinese investments into one of the world's largest and most connected markets. China gets to internationalize its currency through the Grand Duchy, access EU markets and thereby expand its European presence. Luxembourg's solid regulations and expertise in international finance help China expand its global economic influence while safeguarding its European investments.

While Luxembourg continues to serve as a gateway for Chinese financial interests, this role is shaped by complex geopolitical and economic challenges. Luxembourg must navigate between maintaining its beneficial economic ties with China and complying to EU standards and policies. Luxembourg must implement a strategy that balances economic interests with diplomacy, keep the dialogue open and the country's values. China, on the other hand, sees that Luxembourg is an asset and an effective gateway to European markets. The interest in Luxembourg will always be there, despite recent economic fluctuations. China will always see Luxembourg as a financial bridge for its aspirations in Europe.

This mutual relationship reflects broader global financial trends. Luxembourg's success as a small nation with an enormous impact on finance shows that smaller countries can play key roles in global financial networks by using smart partnerships, regulatory expertise, and financial innovation.

To sum up, the economic teamwork between China and Luxembourg demonstrates how smaller nations can have a major impact on international financial movements through proactive and adaptable financial strategies. Luxembourg's ability to attract Chinese investments proves its skill in offering both financial know-how and a safe, progressive environment for international cooperation. This partnership, built on economic and diplomatic ties, sets an example for future global teamwork, emphasizing the growing links between finance, green finance, sustainable finance, diplomacy, and cultural exchange.

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