



INVESTING “OUTSIDE THE BOX”: SHAPING AN INNOVATIVE ASSET CLASS

2026: Blended Finance – where performance meets purpose

Infrastructure financing offers a range of investment opportunities, but risk constraints have traditionally kept investors anchored in developed markets. That boundary is now shifting as blended finance opens more accessible routes into emerging economies.

Exploring a new investment universe with blended finance

Achieving a well-diversified portfolio with an attractive risk-adjusted return and measurable impact can be challenging – particularly when many high-impact opportunities lie in emerging markets that investors may find unfamiliar or difficult to access. And while climate and sustainability have become controversial topics in

some quarters, many investors still prioritise them as part of a sound long-term strategy. This is where blended finance becomes relevant: it can open up investable pathways into markets and projects that might otherwise be out of reach.

“Blended finance focuses on bringing together public and private sector capital in the form of risk-tiered funds that aim to mobilise scalable amounts of private capital into impactful projects in emerging markets.”

In essence, blended finance provides private sector investors with access to emerging markets in a significantly de-risked way while helping them meet their impact goals. A key principle of



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blended finance is that it “blends” the capital, expertise and track record of public and private sector partners. The result is a robust investment opportunity with real-world outcomes.

Blended finance pioneers with proven track record

AllianzGI is one of the very few large asset managers with a dedicated Development Finance team. Since 2017, the team has raised more than USD 4.2 billion in commitments across development finance strategies, typically focused on mobilising capital towards private debt investment strategies that support economic development across emerging markets – including blended finance.

Selecting the investments

How do we select the investments in our blended-finance funds? First, we apply environmental, social and governance (ESG) analysis as the base screening to all portfolio investments. The goal is to identify and assess potential environmental and social risks from the outset. Robust ESG due diligence is essential and requires far more than simply applying an exclusion list.

Second, we evaluate the potential positive impact of an investment, in terms of measurable social or environmental benefits, in the form of its contribution to the UN Sustainable Development Goals (SDGs).¹

While regulatory safeguards have intensified, concerns remain in the market as to which managers and strategies are properly incorporating ESG and impact due diligence. At AllianzGI, we have a dedicated

impact team that supports development finance strategies with ESG due diligence as well as impact assessment (ex-ante and ex-post), in a way that is transparent for investors.

From AllianzGI’s perspective, we consider that consistently implementing robust ESG standards throughout the investment process is essential to drive portfolio performance. This, coupled with a thorough impact screening, is key for the success of Blended Finance vehicles.

Credit enhancement and blending

For investors entering emerging markets, challenges often include regulatory constraints, limited ability to assess risks accurately, and a lack of familiarity or on-the-ground presence. Perceived risks – which do not always materialise – can relate to political context, credit quality, capital convertibility and transferability, tax regimes and other market factors.

To overcome these barriers to entry and manage the risks, close collaboration with development finance institutions (DFIs) and multilateral development banks is crucial. These institutions are pioneer emerging-market investors and still represent the majority of the capital flowing into many of these markets. Investing alongside the DFIs enables investors to leverage their local presence, expertise in sourcing impactful projects, and the privileges that are derived from their the halo effect from the “Preferred Creditor Status”, including withholding tax exemptions and currency convertibility and transferability waivers.

As a result of this expertise, DFIs have a proven track record in emerging markets with very limited credit losses even through challenging economic cycles. This means that even before blending, the target assets can perform better than many investors new to emerging markets might expect.²

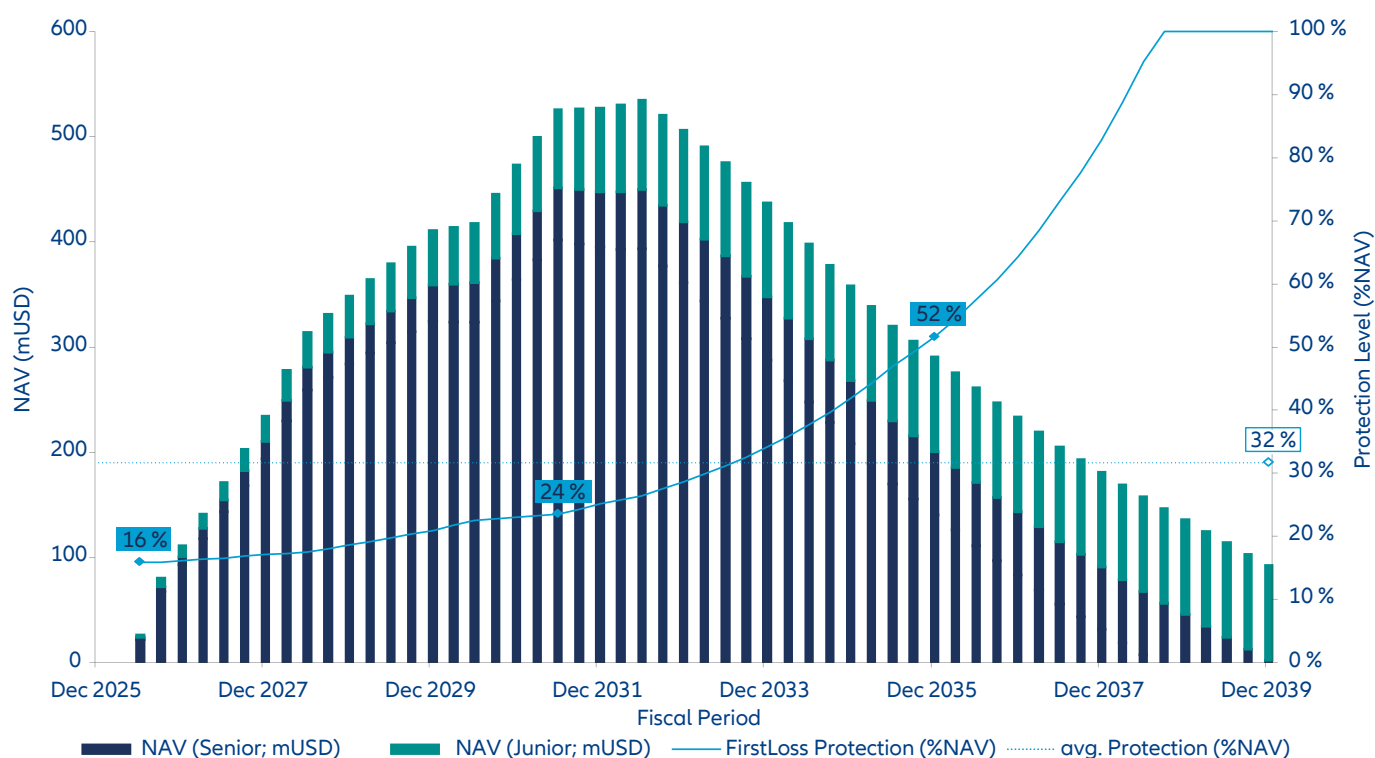
Development Finance Institutions (DFIs)

- As the key investors in these markets, DFIs are highly experienced. Their good relationships with central banks, governments and regulators are beneficial in sourcing investment opportunities.
- These partnerships provide investments with a “halo effect” that can effectively reduce the risk of investments, lowering the probability of default and improving recovery rates.
- DFI partners also keep a portion of the loans on their balance sheet to ensure alignment of interests.
- In addition, DFIs continue to monitor and manage the underlying loans, for example in case of amendments or waivers.

¹ cf. AllianzGI, “**Bringing impact investing into private markets**”, 2023.

² cf., Global Emerging Markets Risk Database (GEMs), “**New statistics from GEMs Consortium Show Risk of Investing in Emerging Markets Is Lower than Commonly Perceived**”, Press release, Oct 7, 2025.

Exhibit 1: Example estimation of first-loss protection and solvency capital requirement (SCR) for illustrative model portfolio



Exemplary estimation of first-loss protection for Illustrative Model Portfolio. The Illustrative Target Portfolio does not represent the portfolio holdings of any account managed by Allianz Global Investors, and there is no guarantee that any account managed by Allianz Global Investors will achieve the investment characteristics described above.

Senior NAV includes share which is protected by the unfunded guarantee (not shown separately).

To mitigate credit risk concerns, we work closely with institutions that provide us with credit enhancement either commercially (eg, via credit insurance) or by raising public sector capital, which provides first-loss protection in a blended vehicle.

For insurers, the former method may be particularly attractive when solvency risk capital is scarce and spreads are tight.

In blended finance structures, public sector agencies typically take a junior position to de-risk senior investors. This enables senior investors to hold a low-volatility position with returns commensurate with the risk. This is possible because the junior investors are prepared to bear a bigger share

of the potential risk. Furthermore, the vehicles have a defined cashflow allocations such that senior investors have priority over underlying portfolio cashflows. Together, these features provide senior investors with downside protection on both return and capital.

For institutional investors and, in particular, insurance companies, these various de-risking measures are essential to achieve an investment grade credit profile and, potentially, reduce capital consumption under the Solvency II framework.

Case study: Downside protection in numbers

Consider a large-scale blended fund with 85% of capital coming

from senior investors, ie, private sector institutions. Junior investors provide 10% of the capital with the remaining 5% covered by an “unfunded guarantee”. Until seniors are fully redeemed, 100% of principal repayments from the underlying debt investments will be distributed to them. We have modelled an illustrative target portfolio of 45 investments to be executed during an investment period of four years, assuming no extensions.

In this example, the senior investors will, at inception, benefit from a first-loss protection of 15.8%³ of invested capital, given their share in the fund structure. As debt repayments come in, the level of protection will increase since the junior capital is not

³ 15% protection over 95% total invested capital.

redeemed. At the projected peak of invested capital (after around five years), the first-loss protection would already represent approx 25% of invested capital. Therefore, even if one-quarter of all investments made were to default, senior investors would not bear any realised losses on their portfolio share. After around 10 years, the protection level would have further increased to more than 50%, eventually reaching full protection once the remaining (senior) principal outstanding is fully covered by the first loss guarantee.

Priority of cashflows: on average, the protection is about double the initial protection level.

Although Solvency II standard model investors may not necessarily benefit from the risk mitigation in their solvency capital requirement (SCR), it is worth noting that the protection levels described above exceed

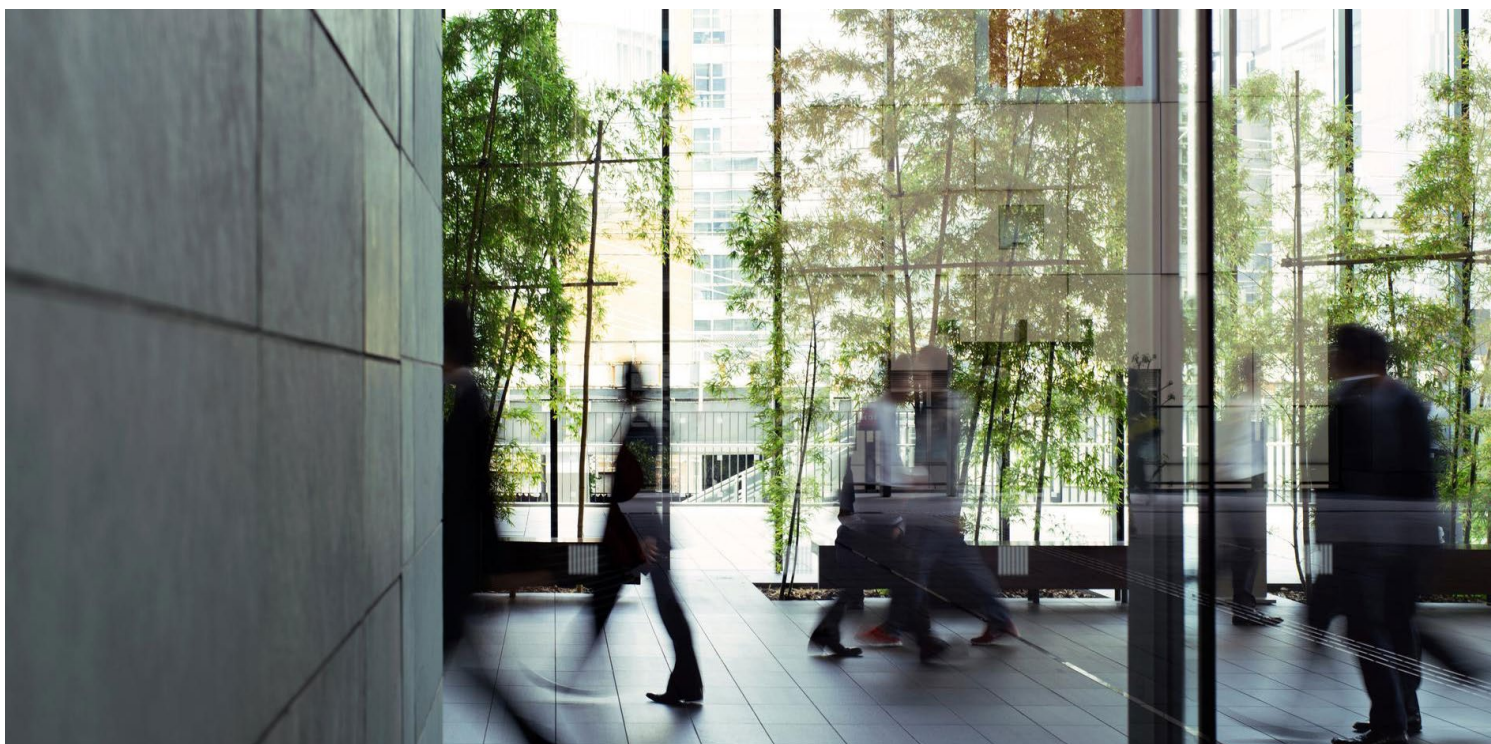
the one-in-200 year event the SCR formulas are aiming to capture.

If necessary, there are ways of structuring these vehicles such that the risk mitigation can be accounted for even by standard model insurers.

To summarise, blended-finance funds can provide investors with a risk-adjusted way to access emerging markets. Investing in sectors and geographies that are underrepresented in public emerging-market indices can be a portfolio diversifier with higher yields. Despite the significant financing needs, capital markets in many of these jurisdictions remain underdeveloped: this is where DFIs and blended finance vehicles come into play. For certain investors such as life insurers, with “illiquid” balance sheets, private markets are the perfect spot to harvest additional illiquidity and in this case

complexity premia.

Blended Finance can be an attractive investment proposition. From the perspective of geographical diversification alone, one can already foresee a low correlation to investments in traditional developed markets. Combined with the significant downside protection mentioned above, the benefits from the preferred creditor status of DFIs, and a yield pick-up versus comparable securities, blended finance can enhance the risk-return profile of the strategic asset allocation of long-term investors. This can be especially true for highly regulated investors like insurance companies, given the increasing risk mitigation over the life of the fund as well as the return targets that aim to generate a meaningful and considerable spread pick-up versus comparably rated securities.



Investing involves risk. The value of an investment and the income from it may fall as well as rise and investors might not get back the full amount invested.

Past performance does not predict future returns. If the currency in which the past performance is displayed differs from the currency of the country in which the investor resides, then the investor should be aware that due to the exchange rate fluctuations the performance shown may be higher or lower if converted into the investor's local currency.

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