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Fiscal Risk Management Circular No: 01/2025

Governor, Central Bank of Sri Lanka
 Secretaries to the Ministries
 Heads of Departments
 Head of the Public Debt Management Office
 Chairman, National Agency for Public-Private Partnership

Roles and Responsibilities for the Preparation of the Fiscal Risk Statement 2026

1. Introduction

- 1.1 As per the provisions of the Public Financial Management Act, No.44 of 2024, and in line with international best practices, this circular stipulates the roles and responsibilities of Ministries, Departments, and relevant Agencies in the preparation of the Fiscal Risk Statement (FRS). The objective is to ensure close coordination among all relevant entities, timely data provision, and efficient assessment of fiscal risks arising from different sources.
- 1.2 This circular applies to all relevant line ministries, departments, and agencies involved in fiscal risk management and reporting, particularly those responsible for macroeconomic forecasting, contingent liabilities, overseeing State-Owned Enterprises (SOEs), natural disasters, and other associated fiscal risks.

2. Understanding Fiscal Risks

- 2.1 For the purpose of this circular, fiscal risks are defined as potential factors that could lead to material deviations in the fiscal position compared to what has been estimated in the Budget and Medium-Term Fiscal Framework (MTFF). Examples include:
 - 2.1.1 Revenue shortfalls due to macroeconomic shocks
 - 2.1.2 Unexpected expenditure pressures such as disaster relief
 - 2.1.3 Contingent liabilities materializing from guarantees or SOE operations
- 2.2 A deviation is considered material if it has a potential fiscal impact exceeding LKR 30 billion (approximately 0.1 percent of GDP).

3. General Responsibilities for All Ministries and Departments

All Ministries and Departments are responsible for:

- 3.1 Continuously identifying potential or emerging fiscal risks within their respective domains that could materially impact revenue, expenditure, or contingent liabilities
- 3.2 Consulting with the Department of Fiscal Policy (FPD) on whether such risks require analysis and reporting for inclusion in the FRS
- 3.3 Alerting the FPD to new or changing risk factors that could impact fiscal outcomes

4. Specific Responsibilities for Nominated Entities for the FRS 2026

The table below outlines the specific roles and responsibilities of nominated entities for the preparation of the 2026 Fiscal Risk Statement. This allocation may be updated for future years as the FRS evolves.

Related Institution	Roles and Responsibilities
Department of Fiscal Policy (FPD)	<ul style="list-style-type: none">- Serve as the agency to consolidate the analysis and inputs in the preparation of the FRS.- Ensure compliance with reporting deadlines.- Prepare the section relevant to fiscal risks arising from macroeconomic factors in consultation with Central Bank of Sri Lanka (CBSL), Department of Inland Revenue, Sri Lanka Customs (SLC) and others if required.- Coordinate and prepare the section relevant to fiscal risks arising from financial sector.- Coordinate and prepare the section relevant to fiscal risks arising from natural disasters.
Department of Public Enterprises (PED)	<ul style="list-style-type: none">- Identify and assess fiscal risks related to SOEs.- Coordinate and prepare the section relevant to fiscal risk arising from SOEs and submit it to the FPD on May 16, 2025.
Public Debt Management Office (PDMO)	<ul style="list-style-type: none">- Coordinate and prepare the section relevant to fiscal risks arising from debt portfolio and guarantees/on-lending and submit it to the FPD on May 16, 2025.- In the medium term, develop and implement a comprehensive framework for assessing the credit risk from loan guarantees and on-lending.
Department of National Budget (NBD)	<ul style="list-style-type: none">- Assist the FPD in preparing the section on fiscal risks arising from natural disasters.
Department of National Planning (NPD)	<ul style="list-style-type: none">- Assist the FPD in preparing the section on fiscal risks arising from natural disasters.

Related Institution	Roles and Responsibilities
	<ul style="list-style-type: none"> - Coordinate and prepare the section on fiscal risks arising from PPPs in collaboration with the National Agency for Public Private Partnership
Central Bank of Sri Lanka	<ul style="list-style-type: none"> - Collaborate and coordinate with the FPD in preparing the section on fiscal risks associated with the financial sector
Department of Treasury Operations	<ul style="list-style-type: none"> - Assist the Department of Public Enterprises to prepare the section on SOEs. - Assist Public Debt Management Office to prepare the section on Guarantees and on-lending.
Disaster Management Center	<ul style="list-style-type: none"> - Provide data and analysis on disaster risk exposure and potential fiscal impacts. - Assist the FPD in preparing the section on fiscal risks arising from natural disasters
Ministry of Environment	<ul style="list-style-type: none"> - Provide inputs on climate change-related fiscal risks for consideration in the FRS

5. Working Arrangements

To facilitate effective coordination:

- 5.1 The FPD and other nominated agencies may form technical-level working groups as needed.
- 5.2 Regular coordination meetings may be held to ensure proper alignment of inputs and timely preparation.
- 5.3 The FPD will provide guidance and technical support to other entities as required.

6. Submission Timeline

To ensure timely compilation of the Fiscal Risk Statement, key milestones are as follows:

- 6.1 Initial risk assessments to be submitted by: May 09, 2025.
- 6.2 Final inputs from nominated agencies due on or before: May 16, 2025.
- 6.3 Draft consolidated FRS to be circulated for review by: May 30, 2025.

7. Reporting Format

- 7.1 All nominated agencies should prepare draft material for inclusion in the FRS 2025 as outlined in Annexure of this circular.
- 7.2 Each section should include: risk description, assessment methodology, quantitative analysis where possible, and risk mitigation strategies.
- 7.3 Accuracy and completeness of data are of utmost importance and any discrepancies should be communicated to the Department of Fiscal Policy at the earliest.

8. Effective Date

This circular shall take effect immediately upon issuance. Ministries, Departments, and Agencies are requested to ensure full compliance and facilitate smooth coordination in the preparation of the Fiscal Risk Statement.



K. M. Mahinda Siriwardana
Secretary to the Treasury

Guideline for the Preparation of Fiscal Risk Statement

Introduction

Fiscal risks refer to the possibility of deviations in fiscal outcomes from what is expected due to various unforeseen events, including macroeconomic shocks, natural disasters, contingent liabilities, state-owned enterprise (SOE) performance issues, and other events that may affect public finances. Identifying, analyzing, and disclosing fiscal risks are essential components of prudent fiscal management. They enable policymakers to anticipate potential challenges, improve fiscal transparency, and enhance the government's ability to respond to economic shocks and manage public resources effectively.

As part of the commitment to strengthen fiscal responsibility and in accordance with the Public Financial Management Act, the Ministry of Finance has initiated the preparation of an annual Fiscal Risk Statement (FRS). This document aims to consolidate and present an overview of the major fiscal risks facing the government and the mitigation measures in place. The following guidelines are issued to relevant agencies to support the timely and comprehensive preparation of inputs to the FRS.

(A) Fiscal Risks arising from the Macroeconomic volatility and uncertainty

- A short analysis of how previous macroeconomic shocks have materialized and have put fiscal plans off-track. It should be supported by quantitative analysis through a forecast error and volatility analysis.
- Main macroeconomic risks facing the Sri Lanka economy looking forward from 2026 and over the forecast period of the FSS/MTFF
- Mitigation measures, such as, the application of fiscal ceilings/ targets and the fiscal reform momentum, measures taken to improve forecasting of GDP, revenue and expenditure, and the contingency buffers

Mitigation measures

- Describe the arrangements that will allow GoSL to better manage macroeconomic risks.
- Brief reference can be made to the new Fiscal Responsibility Framework; the fiscal strategy objectives of revenue mobilization, controlling expenditure growth and rebuilding fiscal buffers; and broader structural reforms to support development of a more diversified economy.
- Specific mention should be made of recent and future steps to address any systematic biases in the forecasting of GDP, revenues and expenditures.

(B) Fiscal Risks arising from SOEs

- Overview of the SOE sector and recent developments

- Aggregated financial information, including a reference to SOEs having negative equity and/or large liabilities
- Distribution of credit risk ratings and analysis of financial indicators for high-risk entities
- Transactions with the government: equity injections, transfers, subsidies, dividends and net flows to the government

Financial performance of non-financial SOEs

- Prepare a summary table presenting the aggregate performance (e.g. revenue, profitability) of the 40 strategically-important non-financial SOEs over the past 3-5 years. Which entities drove the results?
- Include an explanation of how many of the 40 entities were profit-making and how many were loss-making in 2024. Identify any of the 40 entities that recorded negative equity as at the end of 2024.
- Include a chart (see main Report) identifying the SOEs with the largest liabilities and their contribution to the total liabilities of the sector.

SOE Risk Assessment

- Briefly explain methodology has been developed to allow MoF to undertake a credit risk assessment of individual SOEs using financial ratio analysis.
- Present an overview of the risk ratings in a table that lists the number of entities in each risk category (e.g. very high, high, medium, low and very Low risk).
- Identify the entities that have been classified as very high or high risk and the areas of concern.

Budgetary impact of fiscal risks arising from SOEs

- Present a table or chart, covering the past 5-10 years, on the aggregate financial flows from SoEs to the government (e.g. dividends, taxes, levies) and aggregate financial flows from the government to SoEs (e.g. subsidies, grants, capital injections).
- Calculate the net flows each year and present the net flows as a percentage of GDP for each year.

Mitigation measures

- Discuss any specific policy reform measures to mitigate the risks that will be implemented as part of the reform agenda of Sri Lanka. Measures targeted at high-risk SOEs should be emphasized.

- The policy discussion could also focus on SOE governance frameworks and more general steps being taken to improve the financial performance of the sector and/or reduce the risks that government faces.

(C) Fiscal Risks arising from debt portfolio

- This section could include some summary information and a short discussion of the composition of Sri Lanka's public debt portfolio, and relevant targets or metrics under the Medium Term Debt Strategy (MTDS).
- It should avoid duplicating what will be done through the quarterly Debt Bulletin or other reporting against the MTDS.
- A small set of tables and charts could be used to illustrate the term structure of Sri Lanka's debt, domestic vs FX exposures, fixed vs floating interest rate exposures and projections of debt servicing costs. Discuss the main risk factors and how they may affect the budget (e.g. refinancing risk, interest rate risk and exchange rate risk).
- Supplement with information on the latest credit risk assessments and ratings published by the main rating agencies.
- Include an overview of the on-lent portfolio in the first FRS.

Mitigation measures

- Describe the measures that are taken to mitigate debt-related risks.
- These could include the implementation of a prudent debt management policy (i.e., with a reference to the adopted debt management strategy), ongoing monitoring of the portfolio against relevant targets and publication of the quarterly Debt Bulletin.

(D) Fiscal Risks arising from Guarantees and on-lending

Portfolio Analysis

- Provide a breakdown of loan guarantees and on-lending

Newly issued Guarantees and On-lending

- Provide a breakdown of newly issued instruments, their purpose, and alignment with policies.

Risk Materialization

- Discuss historical risk materialization and highlight the past financial year.

Risk Management Strategy

- Discuss the policy framework (mitigation and monitoring), what is being developed, and discuss provisioning in the budget.

(E) Fiscal Risks arising from Public-Private Partnerships (PPP)

- Provide a high-level discussion on PPP related fiscal risks in the 2025 FRS.
- Briefly discuss the nature of government support provided to PPP projects in Sri Lanka.

Portfolio Analysis of PPP

- If data is not readily available, use the information available in public domain (e.g. ADB Public Private Partnership Monitor 2019 and 2023) for this section.
- Include a chart to depict the growth of the PPP portfolio during this period (number of projects which have seen financial close and value of investment) and changes in sectoral composition during the period (e.g. use stacked columns).
- Then briefly mention the number and sectoral composition of PPP projects in the pipeline (NAPPP has the details).
- Legal, institutional and organizational arrangements for facilitation, management and oversight of PPP projects;
- Nature of fiscal exposure – upfront contribution and explicit contingent liabilities created by government guarantees; and Risk mitigation strategy in place for effective risk management

Fiscal Risk Identification

- Provide an overview of the various types of risks identified and an assessment of their likely fiscal impact.
- If sufficient data is not available, mention that as the database grows, this analysis will be further refined to perform detailed assessments.
- If details are readily available, make a brief mention of historical risk materialization i.e. payments made by Government where a contract was renegotiated, or a guarantee called etc. (e.g. Port City Project – renegotiation etc.)

Mitigation Measures

- Discuss the policy framework being designed for mitigation and monitoring of fiscal risks.
- Mention the planned enactment of a comprehensive PPP Law and associated regulations and guidelines, planned institutional arrangements, recording of contingent liabilities, provisioning in the budget and limiting exposure to PPPs, depending on the measures being considered for 2026.

(F) Fiscal Risks arising from the financial Sector

- Provide a summary account and present a small set of Financial Soundness Indicators(FSIs) addressing the overall health – profitability, solvency, liquidity and asset quality – of the financial system. This can be done in consultation with CBSL and Insurance Regulatory Commission (IRC) to select a suitable set of indicators for banking, non-bank lending and insurance.
- Include preliminary FSIs for December 2024 (available from quarterly updates).

Performance of State-Owned Financial Institutions

- Provide a summary narrative and accompanying analysis of trends in performance of state-owned financial institutions. Consider their overall performance – profitability, solvency, liquidity, asset quality etc – and compare the results to sector-wide averages.
- Present a table or chart on the flows from the sector to government (dividends, taxes, levies) and from the government to the sector (subsidies, budget and capital support) over a 10-year horizon (see examples below). Discuss the results and evolution of flows over time.
- Discussing any material examples where state-owned financial institutions perform quasi-fiscal activities (e.g. subsidized loan or insurance programs where the provider is not fully compensated).
- Discussing other examples where material risk exposures may arise (e.g. the provision of reinsurance by National Insurance Trust Fund (NITF) for natural disaster risks creates underlying exposures for government, including implicit risks if the private insurance market is found to be unable to cope with extreme events).

Mitigation Measures

- Drawing on recent CBSL Financial Stability Reviews (FSRs), prepare a high-level discussion of recent policy measures and future steps envisaged to support financial system stability, including establishment of the financial stability fund. The objective is to provide a clear account of coordination arrangements and how systemic risks are being monitored and managed.

(G) Fiscal Risks arising from the Natural Disasters and Climate Change

Natural Disasters

- Report on the incidence of natural disasters in Sri Lanka over at least the past 10 years. This could focus on the number of persons affected by the main types of events as an indicator of their significance, or presenting available data on damages (or economic loss).

Estimates of Fiscal Costs

- Summarize estimates of the fiscal costs associated with natural disasters over the past 10 years. This can draw on previous World Bank/GFDRR and UN ESCAP work.
- Present a table on the estimated fiscal costs from natural disasters with the following categories.

Table : Sri Lanka - Estimated Fiscal Costs of Natural Disasters, by year
(percent of GDP)

	2015	2016	2017	2018	2019	2020	2021	2022	2023	2024	Avg
Direct costs	##	##	##	##	##	##	##	##	##	##	##
Coordination	##	##	##	##	##	##	##	##	##	##	
Relief	##	##	##	##	##	##	##	##	##	##	
Reconstruction	##	##	##	##	##	##	##	##	##	##	
Transfers	##	##	##	##	##	##	##	##	##	##	
Indirect costs	##	##	##	##	##	##	##	##	##	##	##
Insurance	##	##	##	##	##	##	##	##	##	##	
Adaptation/Mitigation	##	##	##	##	##	##	##	##	##	##	
Revenue losses	##	##	##	##	##	##	##	##	##	##	

- Include probabilistic estimates of fiscal costs

Climate Change

- Summarize material from Sri Lanka's NDCs and other sources to explain projections about the impacts of climate change in terms of future frequency and impact of natural disasters.
- Briefly discuss Sri Lanka's mitigation and adaptation priorities and associated costs.

Mitigation Measures

- Appropriations to Ministries responsible for natural disasters (coordination, relief and compensation arrangements, infrastructure) – how do these compare to the observed historical costs
- Virements, the annual budget reserve, constitutional contingency fund and escape clause under the new Fiscal Responsibility Framework – are these sufficient?
- Natural Disaster Fund
- Insurance and other risk transfer arrangements
- Agreements/Contingent Finance Arrangements with Development Partners
- Fiscal buffers – including maintaining a margin for error in terms of fiscal targets (PBT and PEC), reducing debt levels to allow a response to future disasters