

*Gulbin Sultana*

Manohar Parrikar Institute for Defence Studies and Analyses  
[gulbin.sultana@gmail.com](mailto:gulbin.sultana@gmail.com)

*Despite enjoying an absolute majority in the Parliament, overwhelming popular support, and weak opposition, the National People's Power (NPP) administration's first year in office was far from smooth. It confronted internal and external challenges that tested both its resolve and capability, as well as exposed the party's inexperience in governing the country in challenging times. The government succeeded in changing the political culture and demonstrated its strong political will to bring structural reforms by enhancing governance in the country, but effective implementation is still pending. While it managed to sustain the economic recovery process, natural disasters imposed additional fiscal pressures. The government tried to pursue a balanced, pragmatic foreign policy, yet continued to face complex geopolitical and geostrategic challenges. Nevertheless, the NPP government could navigate through these obstacles and ensured political stability in 2025. People are, however, growing impatient for tangible economic results and the fulfilment of promises for systemic change beyond the initial measures.*

KEYWORDS – Sri Lanka; President Anura Kumara Disanayake; Foreign policy; Governance; Political development; Economic development

### *1. Introduction*

The historic political shift marked by the victory of the National People's Power (NPP), a centre-left coalition, in Sri Lanka's 2024 presidential and parliamentary elections generated both optimism and apprehension regarding the prospect for meaningful reform and economic recovery. The year 2025 thus became a critical test for the ruling party to demonstrate its ability to meet public expectations and deliver on its ambitious election

promises. Dispelling many of the doubts raised by its opponents, the NPP government succeeded in maintaining political stability, fostering communal harmony, sustaining economic growth momentum, and securing the goodwill of the international community. However, the outcome of the 2025 local council elections demonstrates that the wave of euphoria that brought the NPP to power has begun to ebb, even though President Anura Kumara Dissanayake's personal popularity endures. While there remains considerable confidence in Dissanayake administration's political will to pursue long-awaited policy reforms, concerns persist about whether it possesses the strategic adroitness and the autonomy to realise its policy vision- «A Thriving Nation, A Beautiful Life» [NPP Manifesto 2024, August]. These concerns have been amplified by the government's handling of climate vulnerabilities and the regional and global geostrategic challenges confronting the country over the past year.

In this background, the paper analyses the political, economic and foreign policy developments in Sri Lanka in the year 2025.

## *2. Political developments*

The policy vision of the NPP government- «A Thriving Nation, A Beautiful Life», according to Prime Minister Haruni Amarasuriya, commits to building a country «where democracy is deepened, where economic justice is prioritised and where voices of the marginalised are not just heard but centred in decision making» [Ministry of Foreign Affairs, Foreign Employment and Tourism- Sri Lanka 2025]. Guided by the policy vision, the government prioritised its focus on improving the governance and changing the political culture of the country. In this regard, the government launched the 'Clean Sri Lanka' programme on 1 January 2025. The 'Clean Sri Lanka' programme is a «holistic undertaking aimed at nation-wide efforts of environmental, social, and governance initiatives to bring about change, integration, and collaboration, in environmental, social and governance structures» [Ministry of Foreign Affairs, Foreign Employment and Tourism-Sri Lanka 2025, 25 February].

## 2.1. *Improving governance*

To strengthen governance, the government launched a National Anti-Corruption Action Plan 2025-2029<sup>1</sup> on 9 April 2025, and enacted the Anti-Corruption and Asset Recovery Act [Office of the Cabinet of Ministers - Sri Lanka 2025, 24 March]. The passage of the long-pending Asset Recovery Act marks a significant milestone in the country's anti-corruption framework, addressing a critical legal gap and empowering authorities to combat illicit enrichment, bribery, and money laundering more effectively.

In pursuit of justice and fairness, the authorities initiated independent investigations and prosecuted alleged perpetrators regardless of their social standing or professional background. Investigations into several longstanding cases have been resumed, including the Easter Sunday attacks, attacks against journalists, and instances of abuse of power by public officials. The government has granted full operational independence to the police, resulting in several landmark convictions [Ministry of Foreign Affairs, Foreign Employment and Tourism - Sri Lanka 2025, 8 September]. Notably, for the first time in Sri Lanka's history, a former president was arrested on allegations of misusing public funds while in office, and an Inspector General of Police (IGP) was dismissed on charges of torture, misconduct, and abuse of power.

The government has leveraged its digitalisation policy to address the issue of corruption and transparency. In this regard, the Digital Roadmap for Sri Lanka (2025–2035) outlines a phased approach to building a digitally competitive nation. Phase 1 (2025–2027) focuses on laying the foundation with a National Digital ID system, the launch of LK-UPI, full digitisation of government payments, 100 per cent smartphone and 4G/5G coverage, and the introduction of DigiLocker Sri Lanka [Muralithas 2025, 24 November].

In addition, to improve governance and transform political culture, the government has prioritised reducing unnecessary state expenditure by curtailing the perks and privileges traditionally enjoyed by politicians, including former presidents.

While these initiatives have earned public approval, they have also sparked criticism. Opposition parties argue that the anti-corruption drive has, at times, amounted to a political vendetta, with selective targeting of individuals while other significant cases remain unaddressed. This criticism intensified following the arrest of former President Ranil Wickremesinghe on charges of misusing public funds during an international tour in 2023. The

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<sup>1</sup> In line with the obligations under Article 5 of the United Nations Convention Against Corruption, Sri Lanka's first National Action Plan against Bribery or Corruption was implemented during the period 2019–2023.

backlash indicates that the government's aggressive anti-corruption drive has unsettled the previously dominant political establishment long associated with systemic political and bureaucratic corruption. According to Prof. Jayadeva Uyangoda [Uyangoda 2026, 7 January], the ongoing transformation of the country's political culture under the NPP government has given rise to an «open confrontation» between the erstwhile «traditional ruling elites and the new ruling party with non-elite social backgrounds».

## *2.2. Enhancing democratic space*

Special attention has been given to expand the democratic space in the country, with a strong emphasis on national unity and the protection of minority rights, including those of women, children, and persons with disabilities. The government asserts that upholding the rights of all citizens—irrespective of gender, ethnicity or other grounds—is a top priority. In this regard, it takes pride in maintaining one of the most inclusive parliaments in the country's history. Women's empowerment, in particular, has received special focus. The current Parliament includes 22 female representatives from diverse social backgrounds, including members of the working class and marginalised communities. Notably, it also marks the first time that two women from the Malaiyaha community have been elected to Parliament [Ministry of Foreign Affairs, Foreign Employment and Tourism-Sri Lanka 2025, 17 February]. Additionally, the cabinet includes specially abled ministers. However, the absence of a Muslim minister in the cabinet raised concerns, although Muslim representation is present at the level of deputy ministers within the NPP government.

According to the Global Democracy Index 2025, Sri Lanka has improved its ranking by 15 positions. Despite this progress, several loopholes remain that need to be addressed to achieve a more inclusive democracy. Public dissatisfaction has grown over the delay in holding provincial council elections, which the government has pledged to conduct in 2026. Furthermore, the government has faced increasing pressure to implement the devolution process as a means of ensuring political rights for the Tamils. Government, however, is non-committal on this issue, citing ongoing considerations of introducing a new constitution. Any such constitutional reform, if undertaken, is unlikely to materialise within the next three years.

## *2.3. Minority rights*

To implement Sri Lanka's commitment under the international mechanism, several legislative reforms have been introduced to advance the rights of children and women. Establishment of a National Women's Commission

under the Women Empowerment Act No 37 of 2024, Sri Lanka's first National Action Plan for Women, Peace and Security for 2023 to 2027, the launch of the Multi-sectoral National Action Plan (NAP) to address Sexual and Gender-Based Violence (SGBV) for the period 2024—2028 and actions taken to address the increasingly challenging issue of online gender-based violence are some of the key policy and legislative reforms introduced by the NPP government in the country [Ministry of Foreign Affairs, Foreign Employment and Tourism-Sri Lanka 2025, 17 February]. The government has announced the drafting of new legislation, including a revised Domestic Violence Bill and a new Disability Rights Bill, to further advance women's rights, children's rights, and the rights of the specially abled person. To further enhance civic space and engagement, the government has announced its intention to bring the national secretariat for non-governmental organisations under the Ministry of Social Empowerment.

For the first time in history, the current government recognised the Malaiyaha community as a distinct community in Sri Lanka. The government is also formulating legislation to facilitate the increase in wages of the plantation sector workers, and it is taking measures to address the housing needs of the community [Ministry of Foreign Affairs, Foreign Employment and Tourism-Sri Lanka 2025, 8 September].

#### *2.4. Tamil reconciliation*

One of the major promises of the NPP government was to focus on Sri Lankan nationalism instead of Sinhala nationalism. The NPP government, which secured overwhelming votes from the north and the east, has pledged to take tangible steps in the interest of further advancing national unity and reconciliation.

The government has initiated confidence-building measures towards reconciliation by addressing key concerns of the Tamil community. The NPP government has upheld the right to commemorate the death of loved ones who lost their lives during the armed ethnic conflict, provided such a right is not misused to glorify terrorism [Ministry of Foreign Affairs, Foreign Employment and Tourism - Sri Lanka 2025, 8 September]. The Cabinet appointed a committee to address land issues faced by people, including conflict-affected people, living in areas identified as forest and other reserves and places of archaeological significance. Around 40.70 acres of land were handed over to the owners by the Sri Lankan Army in Jaffna [Ministry of Defence - Sri Lanka 2025, 8 May]. Several roads in the Northern Province, including the Palali-Achchuveli main road, were opened for public use after several decades, in addition to the launch of several development programmes. The President made an open invitation to Tamil-speaking youth

to be part of Sri Lanka's police service [Ministry of Foreign Affairs, Foreign Employment and Tourism-Sri Lanka 2025, 25 February]. Local civil society organisations, community leaders, and youth groups are participating more actively in dialogue and advocacy than in previous years.

As part of its reconciliation efforts, the government has pledged to strengthen the domestic institutions—such as the Office on Missing Persons (OMP), Office for Reparations, and Office for National Unity and Reconciliation (ONUR)—to address challenges emanating from the conflict, while committing to ensure that these bodies continue to function independently and credibly within the constitutional framework [Ministry of Foreign Affairs, Foreign Employment and Tourism-Sri Lanka 2025, 25 February]. In this regard, the Cabinet decided to allocate Sri Lankan Rs (LKR) 375 million of additional funds to the OMP for the purpose of expediting inquiries into complaints regarding missing persons. The ONUR is in the process of formulating an Action Plan on National Reconciliation with the support of the United Nations Country Office in Sri Lanka. A process has been set in motion to establish and empower a Truth and Reconciliation Commission (TRC) to investigate acts of violence caused by racism and religious extremism that give rise to tensions within Sri Lankan society [Ministry of Foreign Affairs, Foreign Employment and Tourism-Sri Lanka 2025, 25 February]. However, the government has rejected the United Nations Human Rights Council (UNHRC) Resolutions 46/1, 51/1, 57/1 and 60/L.1/Rev.1 and the external evidence gathering mechanism on Sri Lanka.

An important step taken by the NPP government in 2025 was the initiation of an investigation, conducted under judicial oversight and independent of any government interference, into the mass grave sites, including in Chemmani in northern Sri Lanka. To enhance the independence of the Sri Lankan judiciary and the delivery of justice, a decision has been taken to establish an independent public prosecutor's office.

The UK-led Sri Lanka Core Group submitted a report to the UNHRC on 3 March 2025, assessing the country's political and human rights progress. The report praised Sri Lanka's peaceful elections and initial reconciliation efforts, including land returns and eased restrictions in the north and east. Another positive development, as far as reconciliation is concerned, is that there is not much opposition from the Sinhala community to the government's reconciliation efforts. The Sri Lanka Barometer Initiative survey suggests that people are increasingly willing to join reconciliation-related activities. The research, however, finds that «the high public demand for reconciliation is not matched by comparatively modest perceptions of progress» [*Sri Lanka Barometer* 2025].

The government has not yet initiated groundwork on the commitments related to the OMP, ONUR and the establishment of the truth and

reconciliation process. One of the long-pending demands—the repeal of the Prevention of Terrorism Act (PTA)—is yet to be fulfilled. The government has prepared a draft bill called the Protection of the State from Terrorism, aimed at repealing the controversial PTA. People are, however, completely disappointed with the draft.

Jehan Perera, the Executive Director of the National Peace Council of Sri Lanka, has aptly explained the current status of the reconciliation process in Sri Lanka. In his words:

Sri Lanka stands today at a rare intersection of political will, social expectation, and international opportunity. The people voted for a system change. The government has both the power and the legitimacy to deliver. The UNHRC has extended a window for domestic action. Civil society is ready, as the Sri Lanka Barometer confirms, to participate in rebuilding trust. What remains is the political decision to move from intent to implementation. [Perera 2025, 28 October]

Various media analyses suggest that the implementation of many of the confidence-building measures and reconciliation efforts is mostly hindered due to the fragmented politics of the Tamil leaders in the north and east.

## 2.5. *National security*

Sri Lanka experienced a marked rise in organised crime and the proliferation of dangerous drugs throughout the country, while intelligence reports of extremist activities in Kalmunai in the Eastern Province heightened national security concerns [*Tamil Guardian* 2025, 5 March]. In 2025, the country also recorded a significant surge in cybercrime. The Sri Lanka Computer Emergency Readiness Team (Sri Lanka CERT) received more than 12,650 complaints related to cybersecurity incidents and social media misuse during the year [*Newswire* 2026, 1 January].

In response to the escalating drug problem, the NPP government launched the nationwide operation «A Nation United» [President’s Media Division, Sri Lanka 2025, 30 October].<sup>2</sup> It allocated LKR 1.5 billion for drug control programmes and a further LKR 2 billion to address urgent requirements for more efficient prison management [*The Sunday Times*

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<sup>2</sup> This programme is expected to raise social awareness of the threat through a broad campaign, dismantle the networks linked to drug trafficking, strengthen rehabilitation opportunities and offer opportunities for individuals seeking to overcome drug dependence.

2025a, 9 November]. Security agencies intensified surveillance in the Eastern Province to monitor the activities of a suspected religious extremist group. To combat cyber threats, the government introduced the «National Cyber Protection Strategy of Sri Lanka – 2025–2029» in July 2025, which emphasises: upgrading the legal/regulatory framework; enhancing public awareness and knowledge; improving readiness; strengthening incident response; and fostering national and international cooperation [UNODC 2025, 26 October].

Despite these measures, sections of the public have expressed concern that the issue of extremism has not received adequate attention. Similarly, while the government continues its anti-drug campaign, the controversial release of 320 containers from the Colombo Port in January 2025, without comprehensive customs inspection, despite a tip-off from the United States Drug Enforcement Administration (DEA) indicating that two containers in the consignment contained narcotics, has raised questions about the seriousness of its efforts. Further compounding these concerns are contradictory official statements regarding the discovery of alleged «ICE factories» in Nuwara Eliya and claims of selective arrests of individuals involved in the narcotics trade [*The Sunday Times* 2025b, 9 November].

## 2.6. Political challenges

The results of the local council elections held in May 2025, indicate that the NPP does not enjoy overwhelming popular support as it did during the presidential and parliamentary elections in September and November 2024, respectively. Although the NPP secured 266 out of 339 local government (LG) bodies, it failed to obtain an outright majority in 186 councils. Of these, it lacked a clear majority in 149 bodies and was on par with the combined opposition in 29. Consequently, the ruling coalition was able to form administrations in only 116 LG bodies. Collectively, opposition parties won more seats than the NPP. However, their failure to unite against the ruling NPP enabled the government to retain dominance in many local councils. Although efforts were made after the elections to establish a united opposition front, these initiatives failed to gain traction [*The Sunday Times* 2025a, 9 November].

On several occasions, the opposition attempted to move no-confidence motions in Parliament, but these efforts were unsuccessful. At present, the government does not face any significant political challenge. Nevertheless, public support for the NPP appears to be gradually declining. A key source of public dissatisfaction is the delay in tangible economic relief, with many citizens still waiting for meaningful improvements more than a year after the new government assumed office.

### *3. Economic developments*

The resilience of the Sri Lankan economy improved in 2025, due to positive developments in the domestic macroeconomic conditions. The economy grew by 5.0 per cent during the first nine months of 2025 (4.8 per cent, 4.9 per cent and 5.4 per cent in the first, second and third quarters of 2025, respectively) [Central Bank of Sri Lanka 2026, 28 January; Central Bank of Sri Lanka 2025, December; Department of Census and Statistics 2025a]. All three major economic activities—agriculture, industry and service—positively contributed to this growth [Department of Census and Statistics 2025b]. The total government revenue, including tax and non-tax revenue and grants, increased by 24.7 per cent to LKR 2,325.1 billion in the first half of 2025 from LKR 1,864.6 billion in the same period of 2024, realising 46.6 per cent of the annual estimate of LKR 4,990.0 billion. Tax revenue increased by 25.9 per cent to LKR 2,152.1 billion (approximately US\$ 6.95 billion) in the first half of 2025, compared to LKR 1,709.3 billion in the same period of 2024, achieving 46.9 per cent of the annual estimate of LKR 4,590.0 billion. This improvement was primarily driven by the full impact of continued implementation of policy-driven, revenue-based fiscal consolidation measures, enhanced revenue administration, the revival of economic activities, and the lifting of import restrictions, including the removal of the ban on vehicle imports.

Major revenue-earning sectors such as tourism and remittances improved significantly. Tourist arrivals in 2025 surpassed the level recorded in 2018, while recording a year-on-year growth of 15.1 per cent compared to 2024. However, tourist earnings remained below the 2018 level, due to the downward revision of estimates of average expenditure per day and the average duration of stay by Sri Lanka Tourism Development Authority, while recording a marginal growth of 1.6 per cent compared to 2024 [Central Bank of Sri Lanka 2026, 30 January]. The tourism earnings in 2025 were US\$ 3.2 billion. Workers' remittances during 2025 increased by 22.8 per cent on a year-on-year basis, surpassing US\$ 8.0 billion to reach a historic high [Central Bank of Sri Lanka 2026, 30 January].

Total exports, including goods exports and trades in services in 2025, were US\$ 20.6 billion, whereas goods imports were US\$ 21.5 billion. The merchandise trade deficit widened to around US\$ 7.9 billion in 2025, despite export earnings reaching a historically high level [Central Bank of Sri Lanka 2026, 30 January].

Gross official reserves (GOR), including the swap facility with the People's Bank of China (PBOC), improved to around US\$ 6.8 billion by the

end of 2025, even amidst continuous external debt service payments, due to the receipts from multilateral institutions and net forex purchases by the Central Bank of Sri Lanka [Central Bank of Sri Lanka 2026, 30 January].

### 3.1. *Debt profile*

The first condition of the IMF to provide the Extended Fund Facility (EFF) was to restructure the debt to make it sustainable. The debt restructuring was finalised in June 2024 with the Official Creditors Committee (OCC), China EXIM Bank and the International sovereign bond holder by the Ranil Wickremesinghe administration. As per the debt treatment, Sri Lanka received capital grace periods until 2028, reduced interest, and progressive amortisation with final repayments in 2043. Debt restructuring required further efforts through signing mandatory bilateral agreements with key partners. The NPP government in 2025 almost completed the process by signing bilateral debt restructuring agreements with OCC member countries as well as with countries outside OCC. As of the end of June 2025, Sri Lanka concluded the signing of 36 amended agreements covering 194 loans and bonds, with respective development partners and bondholders, and has also shared debt treatment proposals with other bilateral development partners [Ministry of Finance, Planning and Economic Development-Sri Lanka 2025, 31 October].

The external debt of the government as of the end of June 2025 amounted to US\$ 37.1 billion (including multilateral 36 per cent, commercial 34 per cent and bilateral debt at 30 per cent of total government external debt). Total debt service payments during the first half of 2025 amounted to US\$ 1.3 billion. As of the end of June 2025, there were no external payment arrears [Ministry of Finance, Planning and Economic Development-Sri Lanka 2025, 31 October].

During the period from 1 January to 30 June 2025, total foreign loan disbursements amounted to US\$ 547.5 million. The largest share of disbursements was recorded under the IMF's EFF, accounting for 61 per cent of the total. This was followed by disbursements under loan agreements with the World Bank (16 per cent) and the Asian Development Bank (11 per cent). During the first half of 2025, no new commitments were entered into with bilateral, multilateral, or external commercial creditors [Ministry of Finance, Planning and Economic Development-Sri Lanka 2025, 31 October].

The Debt Management Strategy for the period 2025–2029 focuses on a more domestic-oriented financing strategy, maintaining a 80:20 domestic-to-external financing ratio while increasing the issuance of medium-term to long-term treasury bonds to address refinancing and borrowing costs and gradually reducing the reliance on treasury bills. The upward movement in

revenue collection has reduced the fiscal pressure and empowered the treasury to allocate a significant portion of the accumulated cash reserves towards debt servicing obligations, thereby reducing reliance on external borrowings and fostering a more sustainable fiscal environment in the first half of 2025, even though Sri Lanka continued to depend on external financial support to sustain external debt service commitments [Ministry of Finance, Planning and Economic Development-Sri Lanka 2025, 31 October]. However, following Cyclone Ditwah, which struck the country on 28 November 2025, the government has faced a new fiscal pressure, leading to a greater reliance on external financing.

The positive macroeconomic conditions helped the government to provide immediate relief assistance to the victims of Cyclone Ditwah. However, the reconstruction needs have generated significant fiscal pressures and balance-of-payments needs. According to the World Bank, the loss due to the cyclone was about US\$ 4 billion [Central Bank of Sri Lanka 2026, 28 January]. The government passed a LKR 500 billion supplementary estimate to restore the livelihoods of those affected by the disaster. To address urgent balance-of-payments and fiscal pressures arising from the catastrophic cyclone, the government received US\$ 206 million emergency financing under the IMF's Rapid Financing Instrument (RFI) [Central Bank of Sri Lanka 2025, 19 December]. Sri Lanka has also achieved financial assistance from bilateral partners, some of which is in the form of loans. For example, India's US\$ 450 million Ditwah reconstruction package includes US\$ 350 million in concessional lines of credit and US\$ 100 million in grants, targeting restoration of roads, railways and bridges, housing reconstruction, health and education facilities, agriculture support and disaster preparedness [Akashvani News 2026, 8 January].

### 3.2. *NPP's economic reform policy*

The NPP government is continuing the economic reform programme initiated under the Ranil Wickremesinghe administration in line with the IMF requirements. It has adopted a revenue-based fiscal consolidation approach, as prescribed by the IMF, and implemented several policy measures to fulfil these commitments. Consequently, Sri Lanka has received a total of US\$ 1.7 billion so far out of the US\$ 2.9 billion bailout package.

The NPP government, to boost tax compliance and refrain from tax exemptions to maintain support for economic reforms as mandated by the IMF, brought changes in the tax regime since 2025. Effective from April 2025, the exemption on foreign service and foreign source income and the value added tax (VAT) exemption on imported aircraft engines or spare parts was removed. Tax on gains and profits from betting and gaming has been

increased from 40 per cent to 45 per cent. The advance income tax (AIT) rate on interest and discounts was increased from 5 per cent to 10 per cent to enhance tax collection on interest income. The tax-free allowance has been increased from LKR 1.2 million to LKR 1.8 million and the progressive income tax rates applicable to individuals were revised to reflect the revised personal relief. The main changes in the VAT included the abolition of the simplified VAT scheme and replacement by a risk-based refund scheme, and mandatory electronic filing. VAT exemptions were introduced for chemical naphtha supplied to the Ceylon Electricity Board (CEB) and for locally produced dairy products [Inland Revenue Department, Sri Lanka 2025, 17 April]. However, the government has decided to postpone the implementation of 18 per cent VAT on non-resident digital services and the property tax to 2026 and 2027, respectively [Newswire 2025, 5 December].

The loss-making state-owned enterprises (SOEs) are the major contributors to Sri Lanka's fiscal problems. To address the issues faced by the SOEs, the previous government was making plans to privatise them. The NPP government, however, halted the process of privatising the SOEs such as Ceylon Petroleum Corporation (CPC) and CEB. Instead, it is making efforts to restructure them by improving management practices, reducing operational costs, and enhancing efficiency within the existing state ownership structure by initiating cost-reflective pricing in the energy sector. Sri Lanka has a commitment to cost-reflective pricing of electricity not only under the IMF programme, but also under the Sri Lanka Electricity Act, No. 20 of 2009. The CEB is already following a cost-reflective pricing; however, it varies from the methodology used by the IMF to formulate the cost-reflective pricing. Therefore, CEB was not ready to follow the IMF methodology, which the government has already committed to, and thus is having a conflict of interest with the government and is urging the government to renegotiate it with the IMF.

As part of the social safety net, the government has expanded the Aswesuma programme by increasing monthly state sector salaries, wages, social welfare and healthcare allowances.<sup>3</sup> The government is investing in digital transformation to modernise welfare distribution and ensure transparency, with plans to launch a digital identity system to track beneficiaries and eliminate corruption. The government allocated LKR 230

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<sup>3</sup> State sector salaries and wages have increased by Rs. 15,750 (including pensions). The minimum basic salary has been increased from Rs. 24,250 to Rs. 40,000 by including existing allowances into the basic salary. Giving attention to social welfare and healthcare, the monthly allowance for kidney patients and people with disabilities is increased from Rs. 7,500 to Rs. 10,000 and for elderly persons the increase is from Rs. 3,000 to Rs. 5,000. The compensation paid for death or permanent disability due to natural disasters has been increased from Rs. 250,000 to Rs. 1 million.

billion for welfare programmes, a significant increase from previous years [President's Media Division, Sri Lanka 2025, 4 July]. To address the issue of rural poverty and to empower communities and ensure the fair distribution of economic benefits across society, the government launched the «Prajashakthi» National Programme in July 2025 [President's Media Division, Sri Lanka 2025, 4 July].

The IMF believes, «Sri Lanka's ambitious reform agenda is delivering commendable outcomes» [International Monetary Fund 2025, 6 February]. The fourth review of Sri Lanka's four-year EFF program was completed on 1 July 2025. The IMF staff and the Sri Lankan authorities reached a staff-level agreement on the fifth review under the EFF in October 2025, with the expected disbursement of US\$ 347 million by December 2025. However, the fifth review was postponed due to the Cyclone Ditwah disaster. The IMF has offered RFI to Sri Lanka to deal with the disaster crisis.

A section in Sri Lanka is breathing a sigh of relief that the NPP government did not derail the economic growth momentum by rejecting the IMF programme initiated under the previous government. The reform policy could bring macro-economic stability to Sri Lanka, but it did not provide economic relief to the poor. The opposition political parties, particularly the Samagi Jana Balawegaya (SJB), are critical of the view that the NPP government, instead of renegotiating some of the harmful provisions of the EFF, including the austerity measures (as promised during the elections), took over the IMF programme negotiated by the previous administration as it was [Hariharan 2025, 9 March]. It is argued that though the government has made some changes in the tax regime and expanded the social welfare programme as mentioned above, it could not provide relief to the marginalised sections effectively, with the IMF capping of primary expenditure at 13 per cent of GDP and maintaining a primary balance at 2.3 per cent of GDP to address social costs [*The Morning* 2025, 25 February].

### 3.3. *No relief for the weaker section*

Consequently, despite the macroeconomic development in 2025, household incomes, employment, and overall welfare were well below pre-2022 economic crisis levels. A large number of genuinely needy and deserving people are not able to benefit from the government's safety net programmes, such as Aswesuma, due to its ineffective distribution. Research suggests that while Aswesuma transfers may help protect households against low-calorie intake, beneficiary households continue to have low-quality diets, particularly, under-consuming fruits, vegetables, dairy, and legumes [Hülßen et al. 2025]. Even though the government estimates that digitalisation can ensure the effective distribution of the Aswesuma programme, experts

believe that the programme should enhance its ability to target individuals in both chronic and transient poverty, rather than focusing only on chronic poverty [Amarasinghe 2025, May].

The government's price control policy, introduced with the objective of providing economic relief, appears to have generated unintended adverse consequences for consumers. In December 2024, price controls were imposed on rice, a staple commodity. However, the implementation of this price ceiling—combined with an import tariff of LKR 65 per kilogram—contributed to supply distortions in the domestic market. These measures, alongside weather-induced production shortfalls, resulted in significant rice shortages and exacerbated food insecurity and malnutrition in Sri Lanka. The price cap constrained market adjustments to reduced supply, while the import tariff increased the cost of imported rice by an estimated 50 per cent, further limiting affordability. The interaction of these policies fostered the emergence of black-market activities, as formal market channels struggled to meet demand at the regulated price [Seneviratne 2025, 6 February]. Similarly, a salt shortage—attributed to low domestic production and administrative inefficiencies—disproportionately affected low-income households. Collectively, these developments underscore the distributional impact of price controls and trade restrictions, particularly when implemented in the context of supply-side constraints.

To reduce the cost of medicines and to offer long-awaited financial relief to the public, Sri Lanka's parliament approved a new pricing reform for pharmaceutical products, paving the way for the introduction of maximum retail prices (MRPs) and maximum ceiling prices (MCPs) for all medicine categories, excluding those manufactured domestically, in October 2025. The sustainability of the pharmaceutical supply under the new pricing formula has been suspected, leading to serious concern about its impact on the poor in the event of severe medicine shortages [Hasanzadeh 2025, 5 November].

Cyclone Ditwah further worsened the conditions of the poor in Sri Lanka. Around 1,118,929 people and 309,607 families were affected due to the cyclone in November 2025. About 55,747 families were displaced [Disaster Management Center, Sri Lanka 2025, 30 November]. An estimated 462,000 children are among those affected by the cyclone. 6097 houses were fully damaged, and 112,790 houses were partially damaged [Disaster Management Center, Sri Lanka 2025, 31 December]. Half of those cyclone-affected people have limited capacity to cope with disasters due to unstable incomes and high debt stemming from the 2022 economic crisis [Sultana 2026, 8 January].

### 3.4. *Economic challenges*

According to David Sislen, World Bank Division Director for Maldives, Nepal, and Sri Lanka, «to ensure that all Sri Lankans benefit from the recovery, Sri Lanka needs to shift to a higher growth trajectory through the successful implementation of reforms that enhance trade, investment, competition and female labour force participation, among others» [World Bank Group 2025, 23 April]. While the government continues to implement the IMF-mandated reform programmes, several developments in 2025 have created a discouraging outlook for trade growth, the labour market and the country's investment profile.

The Trump administration's tariff policy posed significant risks to Sri Lanka's macroeconomic and social stability. In April 2025, the US imposed a 44 per cent reciprocal tariff, half of the 88 per cent duty Sri Lanka imposes on US imports. Later, it was reduced to 20 per cent with effect from 7 August 2025. The tariff would impact 86 per cent of the products in the country's export basket, removing the competitiveness of those products in the US market. It is estimated that around 300,000 people directly and around 600,000 people indirectly would be affected due to the tariff imposed on Sri Lanka [*Economynext* 2025, 3 April]. Sri Lanka must therefore diversify its export basket. While the government is looking for trade and investment options in the Global South, no breakthrough was achieved in this regard in 2025.

Sri Lanka's investment profile is still vulnerable. Sri Lanka surpassed the US\$ 1 billion foreign direct investment (FDI) mark in 2025, describing it as an early indication of recovering investor interest and changes underway within the institution. However, this level of inflows remains well below the capital required to support sustained economic expansion [*Daily FT* 2026, 28 January]. According to a study by the Lanka Impact Investing Network, Sri Lanka's annual investment demand is estimated at US\$ 7–10 billion to meet sustainable development goals, US\$ 3–5 billion for infrastructure development, and a further US\$ 2–3 billion annually for climate finance. The study also estimates an additional US\$ 695 million funding gap faced by women-led enterprises.

The government is trying hard to attract investors by addressing the governance issues and making the country investor-friendly. However, the government's dealings with some of the existing investors are feared to be sending a negative message to the foreign investors. As part of its policy of transparency in procurement, the government has stopped all government-to-government project proposals. Under the new policy framework, all projects will be pursued through transparent tender procedures [Mohan 2025, 2 August]. As part of this new policy, the NPP government has reviewed

foreign-funded projects in the energy sector signed by the previous government, including the LNG Infrastructure Development and LNG Supply for Power Plant in Kerawalapitiya by Petronet LNG Ltd., and wind farm projects in Mannar and Pooneryn by Adani Group of Energy Limited (AGEL).

The AGEL, which was facing environmental clearance and a case in Sri Lanka's Supreme Court, decided to withdraw from the project when the NPP government appointed a negotiation committee to renegotiate the proposal. As far as the LNG infrastructure development project is concerned, the NPP government awarded the project to the China Harbour Engineering Company (CHEC) without officially cancelling the project with Petronet [Mohan 2025, 2 August]. US\$ 3.5 billion in FDI by Sinopec, a Chinese company, to develop an oil refinery in Hambantota, which began through a tendering process, is also facing delays and risks of being stalled due to prolonged renegotiations on equity, land allocation and market access [Mohan 2025, 2 August]. There is a concern among the experts in Sri Lanka that these kinds of inconsistent, unpredictable, and confusing policies will discourage the investors, even if political and economic stability is achieved. Australian-based United Petroleum, which entered the Sri Lankan market in August 2023 and invested US\$ 27.5 million to take over 150 existing fuel stations and gained the rights to build 50 new ones, decided to withdraw, citing a lack of profitability in the small market [Mudugamuwa 2025, 6 April].

#### *4. Foreign policy developments*

In 2025, Sri Lanka's primary foreign policy focus was securing economic and diplomatic support from bilateral and multilateral partners to address the country's economic challenges, while safeguarding its strategic autonomy. A key priority for the NPP government was completing the debt restructuring process initiated by the previous administration to sustain economic recovery. To restructure the external debt, Sri Lanka's official sector creditors organised into the Official Creditor Committee, a group of 17 countries co-chaired by Japan, India, and France.<sup>4</sup> The Exim Bank of China remained outside of the OCC, and therefore, Sri Lanka had to negotiate debt treatment terms with both groups in parallel, whilst ensuring comparability of treatment between the two groups [Ministry of Finance, Planning and Economic Development-Sri Lanka 2025, 1 January]. Creditors are under no

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<sup>4</sup> The 17 members include Australia, Austria, Belgium, Canada, Denmark, France, Germany, Hungary, India, Japan, Korea, Netherlands, Russia, Spain, Sweden, United Kingdom, United States.

obligation to offer Sri Lanka debt relief; their willingness depends on the good faith demonstrated by both sides, and the presentation of a credible macroeconomic reform plan that realistically restores economic sustainability. Hence, the NPP administration sought to maintain cordial relations, tried to avoid confrontation with any country as much as possible, and proactively addressed creditor concerns. The Janatha Vimukthi Peramuna (JVP)-led ruling coalition shed its anti-India approach, and moderated its stand on Sri Lanka's bilateral engagements with the USA, while maintaining its strong relations with China. Continuing the Ranil Wickremesinghe administration's foreign policy, the NPP administration positively engaged with other Asian countries, Australia, the EU and the multilateral institutions.

Special attention was given to pursuing a balanced policy towards its major competing partners, including India, Pakistan, China, and the USA, to mitigate strategic pulls and pressures. President Anura Dissanayake, however, claims that Sri Lanka is not balancing. In his words, «we don't look at our relations with these important countries as balancing. Each of our relationships is important to us. We work with everyone, but always with a single purpose – a better world for Sri Lankans, in a better world for all» (*The Sunday Times* 2025, 14 December).

#### 4.1. *Relations with India and China*

The commitment of «Fostering Partnerships for a Shared Future» adopted during President Anura's maiden visit to India in December 2024 was sustained in 2025 by increased political, economic, developmental and security cooperation between India and Sri Lanka. Several India-funded projects were inaugurated, and new MoUs were signed to enhance defence, health, agriculture cooperation, and energy and digital connectivity. India once again emerged as the first responder to the crisis by providing humanitarian and disaster assistance in the aftermath of Cyclone Ditwah. Through a combination of investment-based and grant-oriented projects, and multifaceted engagement since 2022, India has positioned itself as a key partner in helping Sri Lanka ease its debt burden while fostering sustainable and long-term economic growth [Ministry of External Affairs, Government of India 2024, 16 December]. Hence, the JVP has notably recalibrated its approach towards India.

India accounted for over 20 per cent of Sri Lanka's tourist arrivals in 2025 [*Akashvani News* 2026, 8 January]. Sri Lanka's merchandise exports to India reached US\$ 334 million during the first four months of 2025, which a nearly 40 per cent surge from the previous year. Overall exports from Sri Lanka rose 12 per cent year-on-year to US\$ 983 million in April 2025.

According to data released by Sri Lanka's Export Development Board, India has been the second-largest destination for the Island's exports after the United States, overtaking the United Kingdom [Akashvani News 2025, 28 May]. India also accounted for as much as 40–50 per cent of foreign direct investment when routed investments are accounted for [Akashvani News 2026, 8 January]. However, as mentioned above, Indian investors in Petronet LNG and AGEL faced issues. While AGEL withdrew on its own, the NPP Government has handed over the LNG project in Kerawalpitiya to a Chinese company without formally cancelling the project with Petronet LNG. The casual handling of issues with investors from the largest development partner conveys a confused foreign policy approach.

Traditional friendship between China and Sri Lanka deepened in 2025 by reinforcing economic ties through debt restructure, renewal of the currency swap agreement and committing the largest FDI project worth US\$ 3.7 billion in Hambantota, as well as strengthening engagement at the party level between the JVP and the Communist Party of China. Nonetheless, the Chinese oil refinery project faced delays due to a lack of consensus on the issues of equity and market access.

The government justified its handling of investment-related engagements with Indian and Chinese investors by emphasising its commitment to promoting transparency and reducing corruption in the energy sector, while rejecting any notion of preferential treatment toward a particular investor. Amid the «progressive thaw» in India–China relations, Sri Lanka was able to navigate its strategic partnerships with both powers with relative ease, avoiding significant external pressures while maintaining balanced ties.

#### *4.2. Navigating the India-Pakistan confrontation*

India-Sri Lanka conflict following the Pahalgam attack in April 2025 and India's Operation Sindoor in May 2025 created diplomatically challenging situations for Sri Lanka. However, Sri Lanka continued to maintain its non-aligned position. Following the Pahalgam attack, President Anura Kumara Dissanayake conveyed a condolence message to PM Modi and strongly condemned the terrorist attack, which claimed 26 lives [President's Media Division, Sri Lanka 2025, 25 April]. Demonstrating Sri Lanka's firm stance against terrorism in all its forms and cooperating with India, the Sri Lanka Air Force (SLAF) conducted a «comprehensive security search» of an aircraft that arrived from Chennai at Bandaranaike International Airport on 3 May 2025 after a tip-off on a suspect connected with the Pahalgam attack being on board the flight. Even though the Government of India accused Pakistan of instigating cross-border terrorism, Sri Lanka refrained from taking any view on it and participated in the scheduled Defence Dialogue

2025 on 27 April 2025 between Sri Lanka and Pakistan in Karachi. No official communication was issued by the Sri Lankan government on the military operations carried out by India and Pakistan during 7–10 May 2025. It was only after India and Pakistan decided to stop all firing and military action on land and in the air and sea on 10 May 2025 that the Sri Lankan President's office issued a «Message of Appreciation» for the leaders of India and Pakistan. During Operation Sindoor, Sri Lanka maintained its neutrality by maintaining its commitment not to allow its territory to be used by any party in the conflict. It is noteworthy to mention here that this policy of non-alignment was not followed by Sri Lanka during the India-Pakistan War in 1971.

#### 4.3. *Relations with the US*

The JVP historically opposed Western and American influence in Sri Lanka. However, ahead of the 2024 Presidential elections, the party initiated engagement with the United States, and following its electoral victory, the government pursued a constructive dialogue, particularly on economic recovery and debt restructuring. Nonetheless, the suspension of USAID programmes and the implementation of US reciprocal tariffs negatively affected key initiatives in food security, economic reform, governance, anti-corruption, border security, and migration management [Alphonsus 2025, 30 March].

In 2024–2025, Sri Lanka was slated to receive US\$ 53 million under USAID, representing 0.07 per cent of gross national income. A survey by the Civil Society Organisations Collective indicated that over 565,000 direct beneficiaries and 400 project staff would be impacted by the suspension [Alphonsus 2025, 30 March]. Reciprocal tariffs further strained Sri Lanka's export sector and job opportunities, although negotiations successfully reduced the tariff from 44 per cent in April to 20 per cent by August 2025.

While seeking a favourable tariff agreement, Sri Lanka adopted a cautious approach to the US military action in Iran, reflecting a shift from the JVP's traditional anti-US stance. Despite reduced collaboration on economic and social programmes, bilateral defence cooperation expanded. Under the Megaports Initiative, the US supplied radiation detection equipment at the Port of Colombo in March 2025. Additionally, a memorandum of understanding formalised defence partnerships between the Montana National Guard, US Coast Guard District 13, and the Sri Lanka Armed Forces through the State Partnership Programme (SPP), institutionalising cooperation in humanitarian assistance, disaster response, maritime security, anti-trafficking, and cyber defence [*The Sunday Times*

2025, 14 December]. Sri Lanka now participates in a global SPP network linking over 115 countries.

#### 4.4. *Expanding partnership*

To continue the halted projects under the USAID programme and also to attract foreign investment, the Sri Lankan government is looking for alternative donors and development partners in the Global South and partnerships with multilateral institutes. The Sri Lankan government, in this regard, engaged with several Asian countries. Japan, which was once the largest development partner of Sri Lanka, has gradually re-intensified its engagement with Sri Lanka. In addition to enhancing their economic partnership, Sri Lanka and Japan have strengthened security and defence cooperation, with Sri Lanka becoming a partner in Japan's official security assistance (OSA) programme in September 2025. Under the OSA programme, Japan offered unmanned aerial vehicles (UAVs) to Sri Lanka for enhancing maritime surveillance and disaster relief capabilities.

Sri Lanka aims to strengthen its partnership with the Association of Southeast Asian Nations (ASEAN) by seeking the status of a Sectoral Dialogue Partner (SDP). The proposal was approved by the Cabinet of Ministers, following a 2019 letter of intent. This status, which allows non-Southeast Asian countries to engage with ASEAN, can enhance Sri Lanka's economic progress and diplomatic relations with ASEAN nations.

As one of the promises of the NPP was to modernise the armed forces with new technology and enhance the country's maritime security, the government in 2025 enhanced its defence engagement with Australia and the UK. Sri Lanka has received a state-of-the-art Shallow Water Multi-Beam Echo Sounder for the Sri Lanka Navy Hydrographic Service (SLNHS) from Australia to develop Sri Lanka's hydrographic capabilities [Sri Lanka Navy 2025, 18 February]. A hydrographic cooperation agreement was also signed between Sri Lanka and the UK [Ministry of Defence-Sri Lanka 2025, 14 February].

#### 4.5. *Foreign policy limitations*

Given the historical ideological baggage associated with the JVP, the NPP's measured diplomacy has mitigated international apprehensions and preserved external goodwill. The government has navigated competing geopolitical pressures with caution, maintaining engagement across major powers. Despite positive engagements with its development partners, it avoided effective engagements with concerned countries on many of the crucial issues of national interest, such as the issue of its claim on the

continental shelf and membership in BRICS. No action has been taken so far on the issue of allowing foreign marine scientific research vessels and thereby affecting marine scientific research in the country. An overly cautious, non-committal posture risks deferring substantive engagement on issues central to national interests, thereby limiting Sri Lanka's ability to shape outcomes in its favour.

## *5. Conclusion*

Governance in Sri Lanka in 2025 under the NPP administration reflects a mixed but noteworthy trajectory. The government entered office with a strong electoral mandate to transform Sri Lanka's political culture and restore public trust in governance. In several respects, it has demonstrated intent to institutionalise financial discipline and recalibrate political norms. On issues such as national integration, the administration has moved beyond rhetoric toward concrete engagement, signalling an attempt to reframe state-society relations. However, while symbolic and procedural shifts are evident, the deeper structural reforms necessary for long-term systemic transformation remain largely uninitiated.

The NPP benefits from an absolute parliamentary majority and a fragmented opposition, conditions that theoretically reduce political constraints on reform implementation. Yet, the limited progress on structural transformation suggests that the principal impediments are not political. Institutional inexperience, limited technocratic depth, and an absence of long-term policy coherence appear to have constrained reform momentum. Moreover, policy inconsistency—particularly in balancing transformative rhetoric with pragmatic governance—has created tensions between electoral expectations and policy delivery. The government now faces the challenge of reconciling ambitious campaign promises with the realities of institutional reform.

Systemic transformation in Sri Lanka cannot be achieved through executive will alone. It requires coordinated action across state institutions and sustained societal support. Despite its anti-corruption emphasis, the administration has encountered institutional friction. This underscores the structural limits of reform efforts in the absence of alignment among key governance institutions.

In the economic domain, policy continuity rather than rupture has defined the year 2025. The NPP government has maintained its commitment to the recovery programme initiated under former President Ranil Wickremesinghe, signalling policy predictability to both domestic and international stakeholders. However, economic stabilisation alone does not

guarantee resilience. In 2025, there were no significant structural initiatives aimed at strengthening shock absorption capacity, broadening the productive base, or advancing export diversification. Inconsistent signals on investment policy and limited progress in transforming the export structure raise concerns about the sustainability of growth and the country's capacity to transition from stabilisation to structural transformation.

On the foreign policy front, the NPP government has performed relatively well in 2025. Through a pragmatic and calibrated approach, it earned external goodwill and managed to navigate strategic pressures from competing regional and global powers. However, in attempting to maintain friendly relations with all and avoid offending anyone, the government is avoiding necessary but difficult discussions with key partners. The concern, therefore, is that over time, such restraint could constrain Sri Lanka's capacity to proactively shape outcomes in alignment with its strategic objectives.

Overall, the government's approach has been cautious and incremental rather than disruptive. While economic and foreign policy continuity with the previous administration is evident, the political domain reflects a perceptible shift in governance style and discourse. Whether these incremental adjustments will culminate in structural transformation or remain confined to procedural reform will depend on the government's ability to institutionalise change over the coming years.

Meanwhile, public perception in 2025 reflects both emerging frustration and guarded optimism. The local council election results suggest that while voters were hesitant to grant the NPP an unqualified endorsement, they have not consolidated around an alternative political force. Delays in implementing key reforms and concerns regarding appointments to important positions based on party loyalty are eroding the moral high ground upon which the NPP's electoral success was built. Nonetheless, given that this was only one and a half years of governance, segments of the electorate remain willing to extend a conditional mandate, contingent upon visible progress in the near term. The year 2026 will therefore be crucial for the NPP's political future, as citizens expect tangible progress on election promises.

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