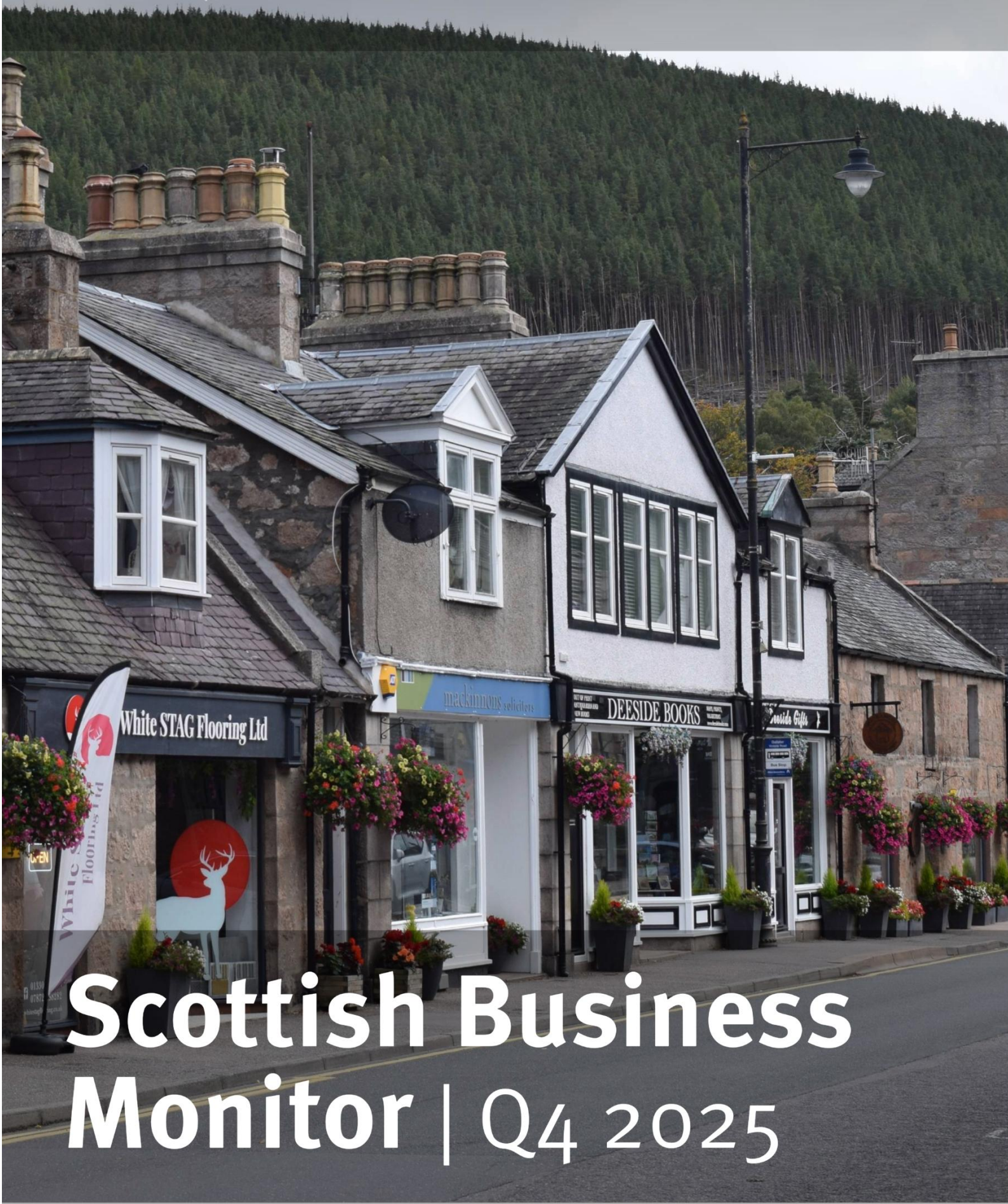




UNIVERSITY of STRATHCLYDE
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Scottish Business Monitor | Q4 2025

Introduction & Summary

Business confidence in Scotland remains weak, with firms pointing to cost pressures, subdued investment, and little prospect of short-term relief as Artificial Intelligence usage becomes increasingly widespread.

This report presents the key results from the Fraser of Allander Institute's (FAI) latest *Scottish Business Monitor* for the fourth quarter of 2025. Over 250 business responded, tracking business sentiment from across all 32 Scottish local authorities

All six headline indicators in the quarterly survey, have remained in negative territory for a fifth consecutive quarter. This degree of persistence, rarely seen in the series dating from 1998, suggests that pessimism is becoming entrenched rather than transitory.

The report finds labour market conditions continue to soften. **In the final three months of 2025, more businesses reported a decline in employment level, aligning with official data showing nearly 15,000 fewer employees on Scottish business payrolls in November 2025** compared with a year earlier. Firms also reported weaker turnover during the period, including through the traditionally strong 'golden quarter'.

Cost pressures remain the dominant concern: **nearly 80 per cent of firms reported higher total costs in recent months, while around 90 per cent expect costs to rise further over the first half of 2026.**

Despite easing input and energy price pressures, businesses continue to face rising wage and employee costs – a particular challenge in an economy where services account for close to 80 per cent of output and labour costs are a key driver of inflation.

Looking ahead, the survey highlights continued weakness in both new capital investment and export activity. While access to credit is not seen as a major constraint, economic and political uncertainty is weighing heavily on decision-making.

More than 9 out of 10 firms cited economic and business uncertainty as “important/very important”, whilst the cost of credit had risen for fewer than half of firms. This suggests businesses are reluctant, rather than unable, to commit to new investment opportunities amid a subdued economic environment.

There are, however, some early signs of adaptation. Almost half of surveyed businesses reported using artificial intelligence in some capacity in the final quarter of 2025, with adoption extending beyond services into construction, manufacturing, and production. The productivity implications of AI, including whether it complements or substitutes for labour, will remain a key area of focus in future analysis.

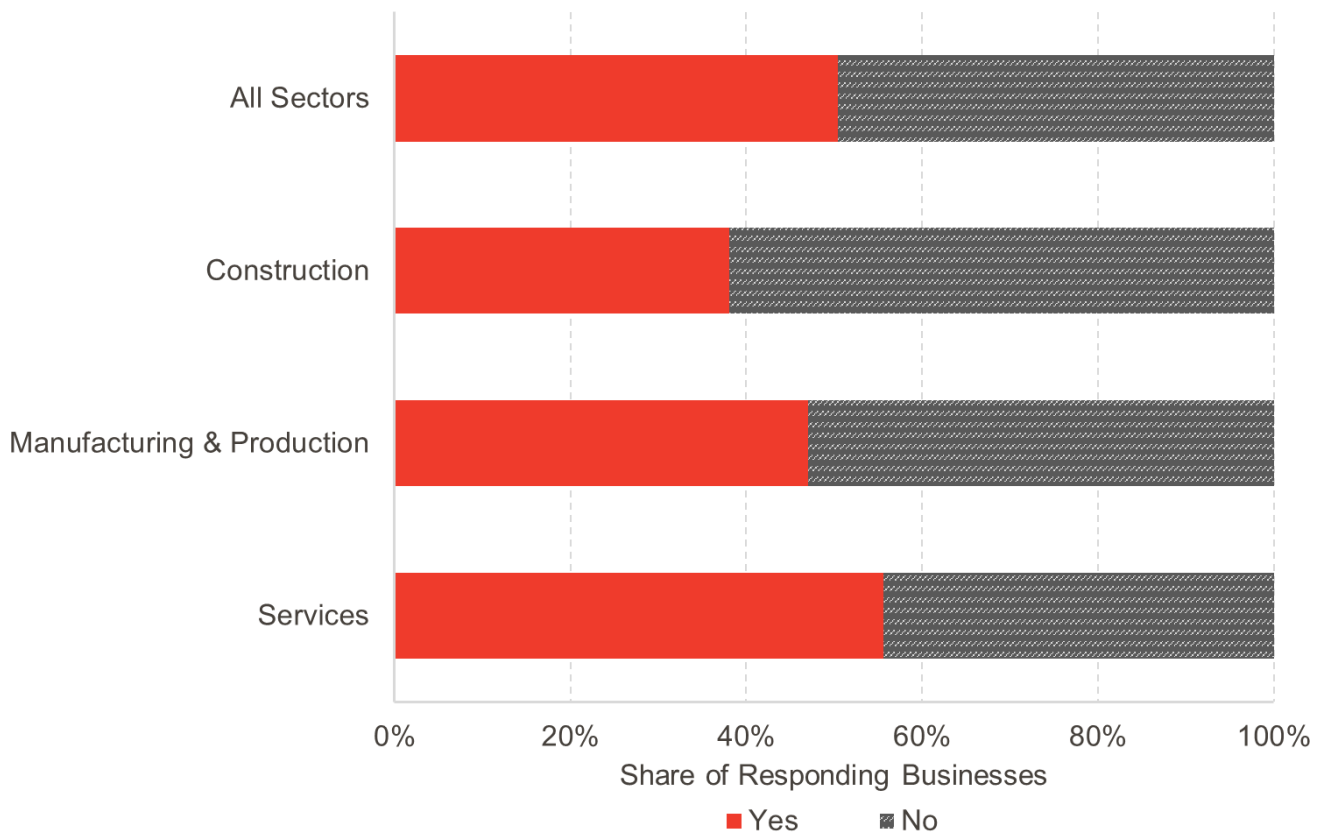
João Sousa, Deputy director at the Fraser of Allander Institute, said “As political parties set out their economic priorities, the Scottish Business Monitor provides a timely snapshot of the conditions firms are experiencing on the ground.

“Persistent cost pressures, weak investment and heightened uncertainty underline the importance of policy clarity and stability if confidence is to recover.

Artificial Intelligence (AI) Usage by Sector

Half of Scottish businesses used AI in their operations in the last 3-month period, with adoption visible across all major sectors.

Chart 1: In the past 3 months, has your business used artificial intelligence (AI) in its operations?



Source: SBM

Artificial intelligence (AI) use among Scottish businesses was widespread this quarter, with **50.4% of all responding firms reporting that they had incorporated the technology** into their operations.

Sector-level analysis reveals that firms in the services industry are most likely to use AI – with 55.6% reporting use in the past 3-months – it’s **adoption is not confined to services-based businesses.**

Evidence of AI use is now visible across most sectors of the Scottish economy. Firms in the construction, manufacturing, and production industries reported healthy levels of AI adoption, despite traditionally being resilient to digital technology. In particular, **38.1% of**

construction firms reported having used AI in the final quarter of 2025.

This suggests a gradual and broad diffusion of AI throughout Scotland’s economy, with adoption cutting across sectoral distinctions.

Although the long-term effects of AI adoption remain uncertain, there are some encouraging signs. As firms continue to explore applications of the technology as a general-purpose innovation, AI could contribute to productivity improvements across the economy.

Ongoing monitoring will be important to understand how adoption patterns evolve and how businesses adjust their operations in response to AI use.

Net Balance of Current Business Activity

This is the fifth consecutive quarter in which all six headline indicators are negative.

Table 1: Net balance of firms experiencing increased activities over the past 3 months, 2023Q1 – 2025Q4

	2023			2024				2025			
	Q1	Q2	Q3	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4
Volume of Business Activity (i.e., Sales)	9.1	3.0	-1.2	-7.1	4.5	-0.8	-8.8	-20.7	-12.8	-12.3	-8.6
Volume of new business activity	5.7	0.0	-9.6	-13.5	-4.2	-1.4	-18.0	-27.4	-13.4	-16.0	-14.0
Value of business activity (i.e. turnover)	8.1	3.7	0.0	-2.6	5.4	3.4	-7.9	-16.2	-10.3	-11.4	-14.6
Level of employment in your business	-0.5	2.2	1.9	-0.3	-2.7	3.9	-8.3	-18.3	-9.9	-8.5	-13.9
Level of new capital investment	-4.4	-12.1	-16.7	-12.1	-10.5	-5.4	-21.6	-26.6	-18.6	-20.4	-25.0
Export activity	-8.4	-11.4	-11.5	-16.4	-10.5	-11.3	-17.2	-16.6	-25.3	-16.6	-20.7

* Net balance of firms is defined as the share of firms reporting 'higher' minus the share of firms reporting 'lower'.

The volume of business activity (i.e. sales) has risen to -8.6%. Although still a negative balance **this is an increase of 3.6 percentage points from the previous quarter** which represents a hastening of the rate of recovery seen in the recent quarters.

Similarly, the net balance **of new business activity experienced an increase of 2.1 percentage points**, although remains in negative territory. Unlike the gradual recovery exhibited by sales, **this indicator has fluctuated within negative territory throughout 2025**, alluding to difficulty creating new and persistent demand.

Whilst the volume of activity improved this quarter, **the value of business activity (i.e. turnover) has slipped by 3.2 points to a net balance of -14.6%.** This continues **the trend of the net balance of turnover decreasing throughout 2025**, after a small recovery in Q2.

This is symptomatic of a weak economic environment where the volume of sales can

recover but fail to convert into a recovery of the total value of said sales.

Levels of employment have fallen by 5.4 points to a net balance of -13.9%. This is consistent with a decrease in the level of pay-rolled employment across the UK labour market, **which our Q4 Quarterly Economic Commentary explores in greater detail.**

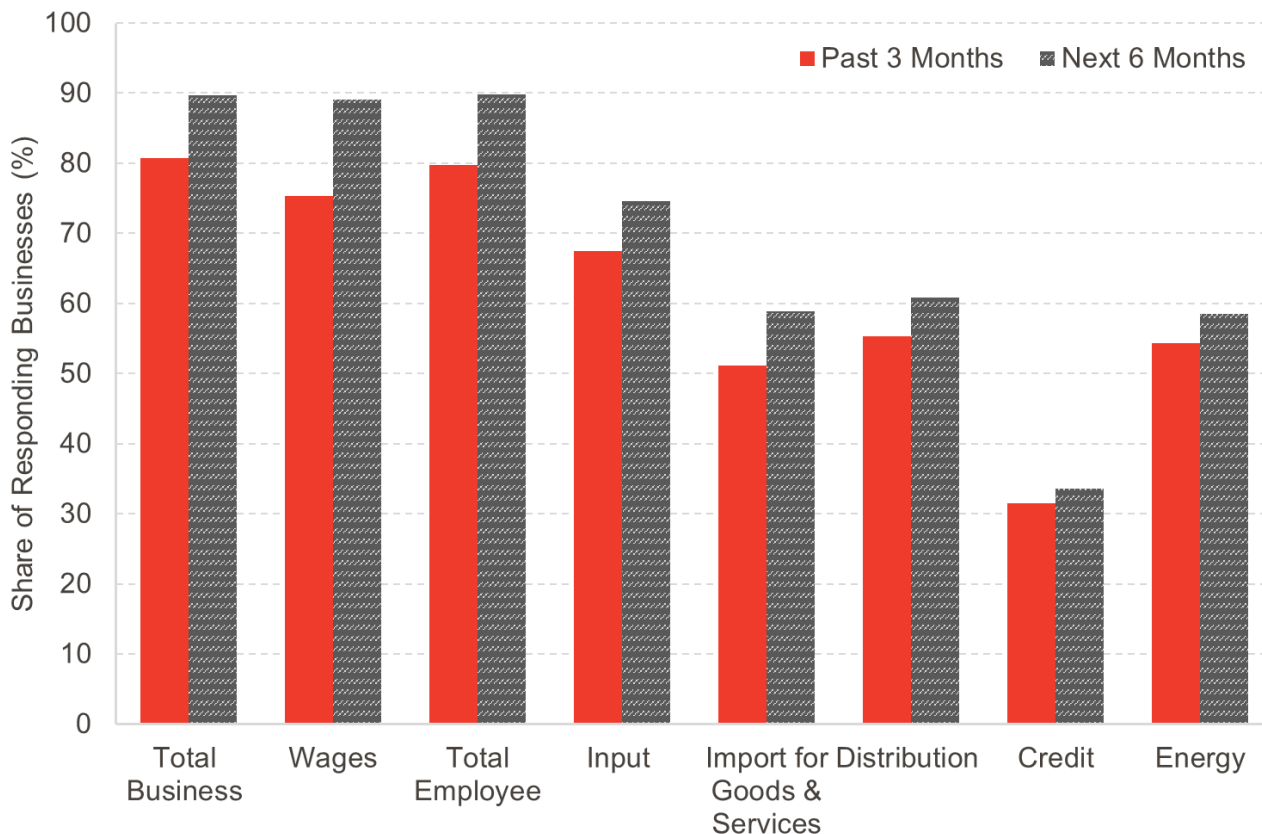
The level of new capital investment is once again subdued, decreasing 4.6 points from last quarter to a low net balance of -25.0%. Reconciled with uncertainty being a greater concern than the cost of credit (explained later in this report) **would suggest businesses are reluctant to make investments, rather than unable to afford them.**

Finally, export activity continues to fluctuate with a double-digit, negative net balance. Declining 4.1 points to a balance of -20.7% from the last quarter. Given the current trade environment, this is not surprising.

Cost Pressures

Cost pressures persisted in Q4 and anticipations signal an uneasy start to 2026 as nearly 9 in 10 firms expect cost pressures to increase further.

Chart 2: Proportion of respondents assessing costs as 'higher' in the previous 3 months and next 6 months, 2025Q4



Source: SBM

Cost pressures were broadly unchanged this quarter, **with the share of businesses reporting higher total costs increasing slightly: rising from 78.4% in Q3 to 80.7% in Q4.**

Looking at individual cost categories, pressures were also largely stable relative to last quarter:

- **Credit costs were the only category in which fewer than half of responding firms reported an increase in Q4,** suggesting affordability is not the constraining factor on investment levels.
- Total employee costs (inc. wages, pensions, NICs etc) continue to represent the most significant individual pres-

sure, with 79.8% of firms reporting higher employee costs this quarter.

Looking ahead to the next 6 months shows a large share of businesses anticipating increases in their total costs, with **89.7% of firms expecting increased pressure in the first half of 2026.**

This pattern is also reflected across every component within the cost category: pointing to a situation where businesses will have to focus on maintaining margins to survive.

UK inflation remains the highest amongst major developed economies despite a sluggish growth environment indicating a difficult start to 2026 is expected by many businesses.

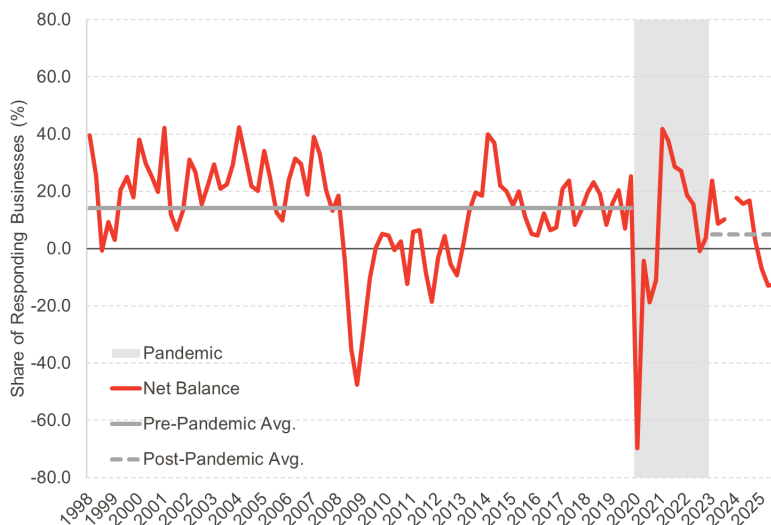
Concerns, Outlook, & Sentiment

Business sentiment has improved from Q3, with **expected sales over the next 6 months increasing by 5.1 points to a net balance of -7.5%**, pointing toward a recovery in sentiment levels, after a mid-2025 slump.

Although still in negative territory, if this trend of recovery continues in future quarters, it may lead to recovery in business optimism and provide reprieve amidst a difficult cost pressure environment.

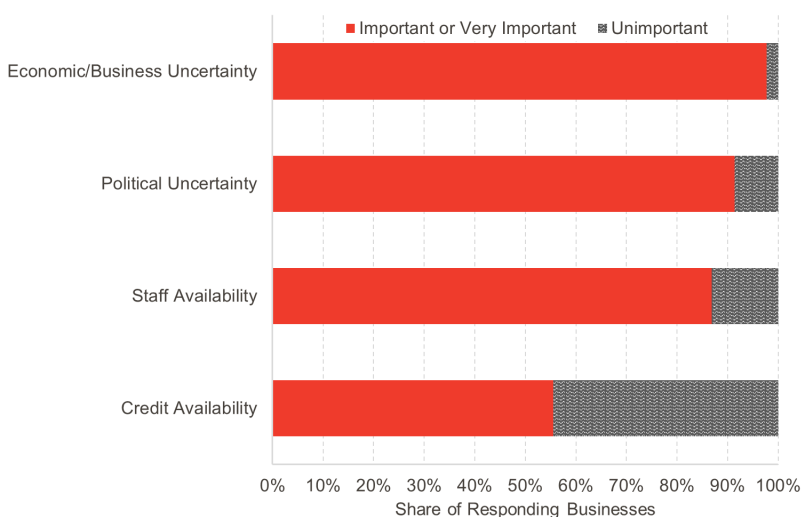
The post-pandemic trend in net balance of expected sales averages 5.1% compared to 14.3% pre-pandemic.

Chart 3: Net Balance of Expected Increase in Sales in the next 6 months, 1998Q1 - 2025Q4



Source: SBM

Chart 4: Concerns of Business over the next 3 months, 2025Q4



Source: SBM

Economic & Business uncertainty was the most important concern, with 97.7% of firms ranking it “important/very important”.

Political uncertainty was also ranked as important /very important by more than 9 out of 10 businesses.

Given the non-domestic rates revaluation in April 2026, and this edition of the SBM surveying before the Scottish Government’s budget, this is unsurprising.

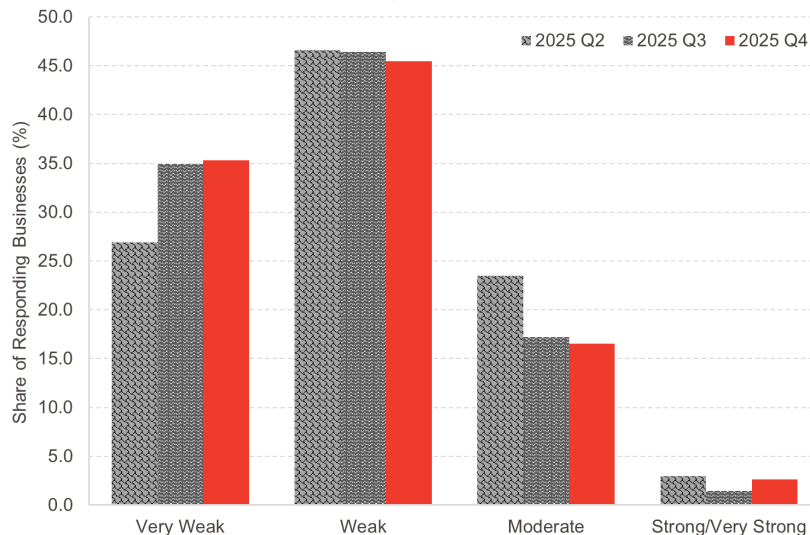
Levels of concern regarding staff and credit availability align with trends already highlighted in this report.

Growth expectations for the next 12 months improved, with the share of firms expecting strong or very strong growth rising by 1.2 points to 2.6%.

However, there has also been a small rise in the share of firms expecting very weak growth, increasing by 0.4 points.

Despite marginal improvements expectations for weak and moderate growth remain most common which reflects a subdued growth environment for most businesses operating in the Scottish economy.

Chart 5: Expectations for Economic Growth over the next 12 Months in Scotland’s Economy, 2025Q2 - 2025Q4



Source: SBM