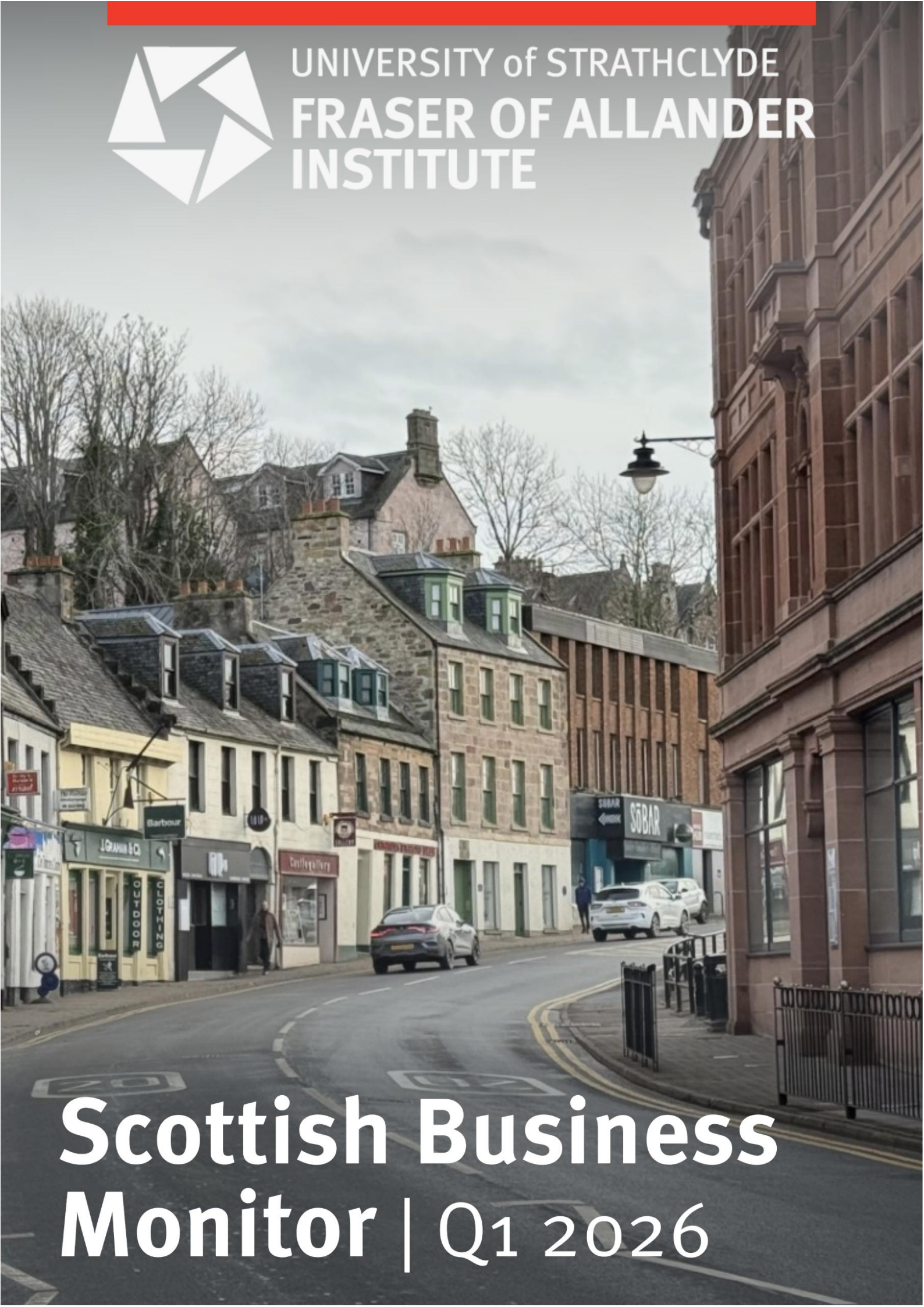




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# Scottish Business Monitor | Q1 2026

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## Introduction & Summary

The Scottish economy entered 2026 with little evidence of a meaningful recovery in underlying activity. The latest Scottish Business Monitor (SBM) results point to a continued divergence between weak real performance and more resilient nominal outcomes, as firms navigate a difficult environment shaped by persistent cost pressures and subdued demand.

All six headline indicators remain in negative territory for a sixth consecutive quarter, signalling that current weakness is broad-based rather than confined to specific sectors. Continued softness in investment and export activity suggests that both long-term confidence and external demand remain under strain. At the same time, the modest improvement in turnover relative to sales points to price-led revenue support rather than a recovery in volumes, raising questions about the sustainability of current business conditions.

Despite this, business sentiment has turned marginally positive for the first time since late 2024. This divergence between expectations and current conditions is indeed notable. It suggests that firms may be anticipating a stabilisation in the economic environment, potentially driven by expectations of easing financial conditions or an adjustment to a lower baseline of activity, rather than responding to a clear improvement in demand.

Cost pressures remain a defining feature of the current landscape. A growing share of firms report increases across a wide range of cost categories, particularly energy, imports, and distribution. This breadth of cost increases limits firms' ability to absorb shocks and increases the likelihood of further pass-through to prices or downward pressure on margins.

At the same time, structural shifts continue to emerge beneath the surface. The latest SBM results suggest that artificial intelligence adoption is no longer confined to early adopters, with evidence of broader diffusion across sectors. While still at an early stage, the extent to which this translates into measurable productivity gains will be a key determinant of medium-term economic performance.

Taken together, the results point to an economy characterised by weak real activity, persistent cost pressures, and fragile but improving expectations. The balance of evidence suggests that current conditions are better interpreted as a period of stabilisation at a low level of activity rather than the beginning of a sustained recovery.

## Headline Indicators & Sentiment: Net Balance

This is the sixth consecutive quarter in which all six headline indicators are negative, pointing to a broad-based weakness rather than sector specific weakness, with falling sales and persistent cost pressures weighing on activity.

**Table 1: Net balance of firms experiencing increased activities over the past 3 months**

	2024			2025				2026
	Q2	Q3	Q4	Q1	Q2	Q3	Q4	Q1
Volume of Business Activity (i.e., Sales)	4.5	-0.8	-8.8	-20.7	-12.8	-12.3	-8.6	-11.6
Volume of new business activity	-4.2	-1.4	-18.0	-27.4	-13.4	-16.0	-14.0	-13.7
Value of business activity (i.e. turnover)	5.4	3.4	-7.9	-16.2	-10.3	-11.4	-14.6	-14.1
Level of employment in your business	-2.7	3.9	-8.3	-18.3	-9.9	-8.5	-13.9	-12.4
Level of new capital investment	-10.5	-5.4	-21.6	-26.6	-18.6	-20.4	-25.0	-19.1
Export activity	-10.5	-11.3	-17.2	-16.6	-25.3	-16.6	-20.7	-22.4

\* 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 (sales) declined by 3.0 points to a net balance of -11.6%, reversing the modest improvement seen in the previous two quarters. The reversal suggests that early signs of stabilisation were not sustained, reinforcing the fragility of underlying demand.

Meanwhile, the volume of new business activity remains broadly stagnant, increasing slightly from a net balance of -14.0% last quarter to -13.7% at the start of the year.

The value of business activity (i.e., turnover) has increased by 0.5 points to a net balance of -14.1% this quarter. When reconciled with the declining sales volumes, this suggests that nominal revenues are being supported by price increases rather than underlying demand strength.

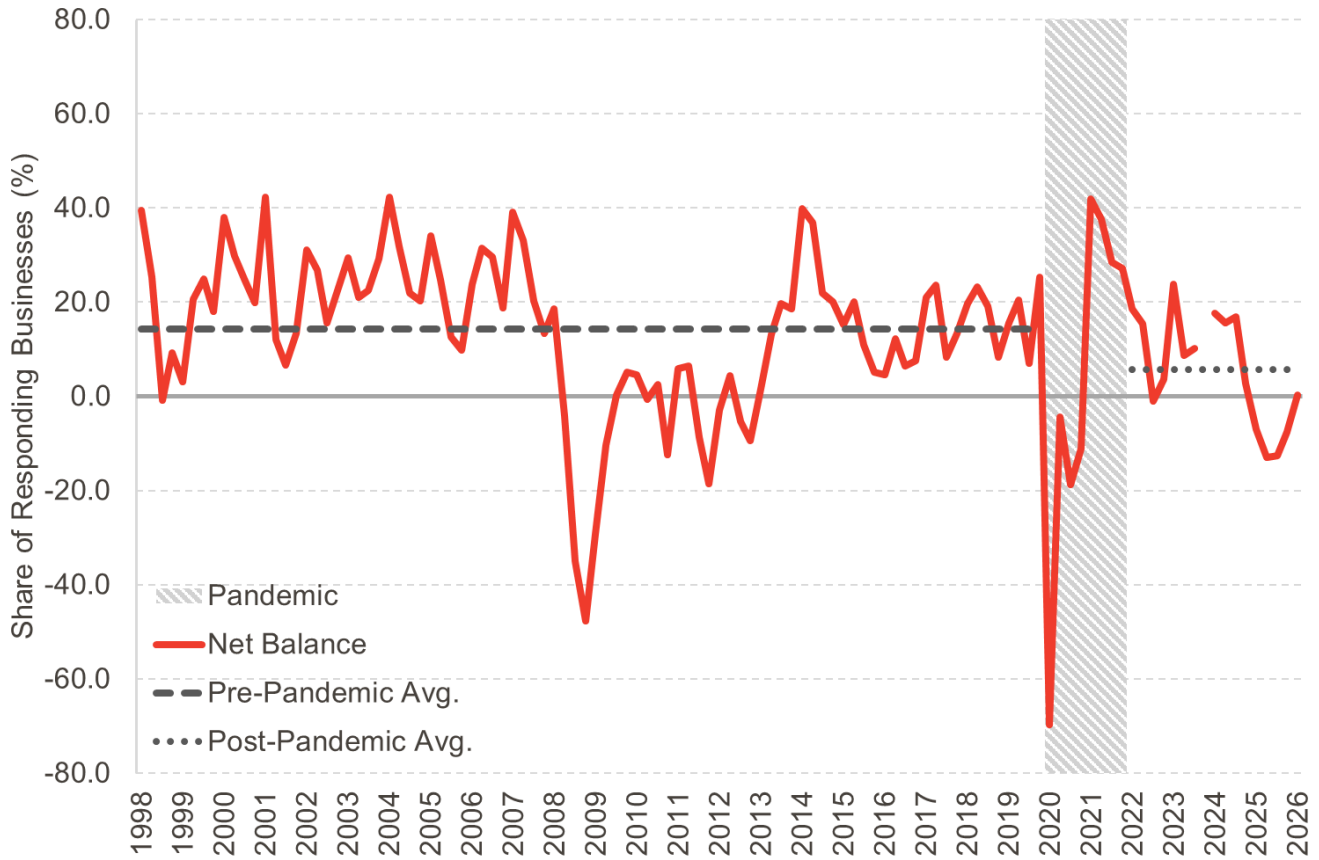
As this wave of SBM was conducted at the outset of the conflict in the Middle East, businesses were unlikely to have fully incorporated resulting cost pressures into their responses. As such, the results reflect underlying domestic conditions rather than the full impact of geopolitical shocks.

The level of employment in businesses has increased by 1.5 points from the end of last year, to a net balance of -12.4% in Q1. With the survey period ending just before increases to the National Minimum Wage took effect, increases in employment are notable especially given the economic data around [the evolution of pay-rolled employees](#).

The level of new capital investment has improved modestly, by 5.9 points, to a negative net balance of -19.1% this quarter. While this represents a tentative improvement in an area of longstanding weakness, more evidence will be required to signal greater certainty about how sustainable the recovery is given prevailing economic conditions.

Export activity remains subdued, slipping by 1.8 points to a new net balance of -22.4 per cent this quarter. This continued weakness is consistent with ongoing volatility in global trade conditions with a plethora of supply shocks hitting businesses all at once.

**Chart 1: Net Balance of Expected Increases in Sales in the Next Six Months, 1998Q1 – 2026Q1**



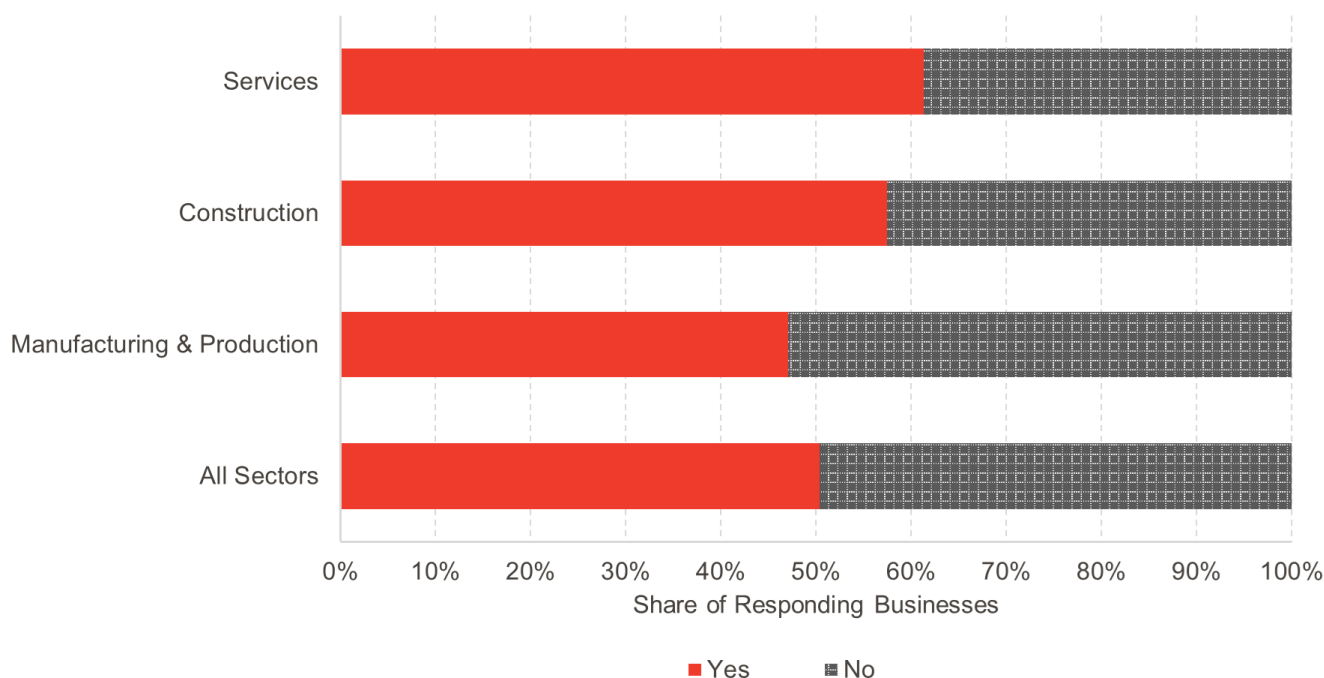
Despite all six headline indicators remaining in double-digit negative territory, business sentiment continued to improve in the first quarter of 2026: rising 7.9 points from the end of 2025 to a new net balance of 0.4 per cent.

Although considerably lower than the pre- and post-pandemic averages (of 14.3 per cent and 5.8 per cent, respectively) this marks the first positive reading since 2024 Q4 in which the net balance of businesses expecting an increase in sales over the next six months is in positive, implying a majority of businesses expect sales to rise over the next six months.

Reconciling this with the headline indicators suggests a divergence between current conditions and expectations. This divergence suggests that expectations may be driven more by anticipated stabilisation than by current economic conditions which can still be characterised as challenging.

## Artificial Intelligence (AI) Usage by Sector

**Chart 2: Share of businesses reporting use of AI in the past three months, 2026Q1**



While overall AI adoption remains at around half of firms, the more significant shift is the broadening of adoption across sectors.

In the previous Scottish Business Monitor, just over half of firms reported using AI, and the latest results show a similar overall figure of around 50%. However, the sectoral results suggest that AI adoption is becoming more widespread across the economy, particularly in sectors such as construction and manufacturing, which have traditionally been slower to adopt new digital technologies. The relatively high adoption rate in construction firms suggests that AI is increasingly being used for project planning, cost estimation, scheduling, design, and administrative processes.

This pattern is consistent with the way new technologies typically diffuse through the economy. Early adoption tends to be concentrated in services and technology intensive sectors, but over time adoption spreads into more traditional and operational sectors as tools become cheaper, easier to use, and embedded in standard business software.

The Scottish Business Monitor results suggest that AI adoption in Scotland may now be moving from an early adoption phase towards broader economy-wide diffusion.

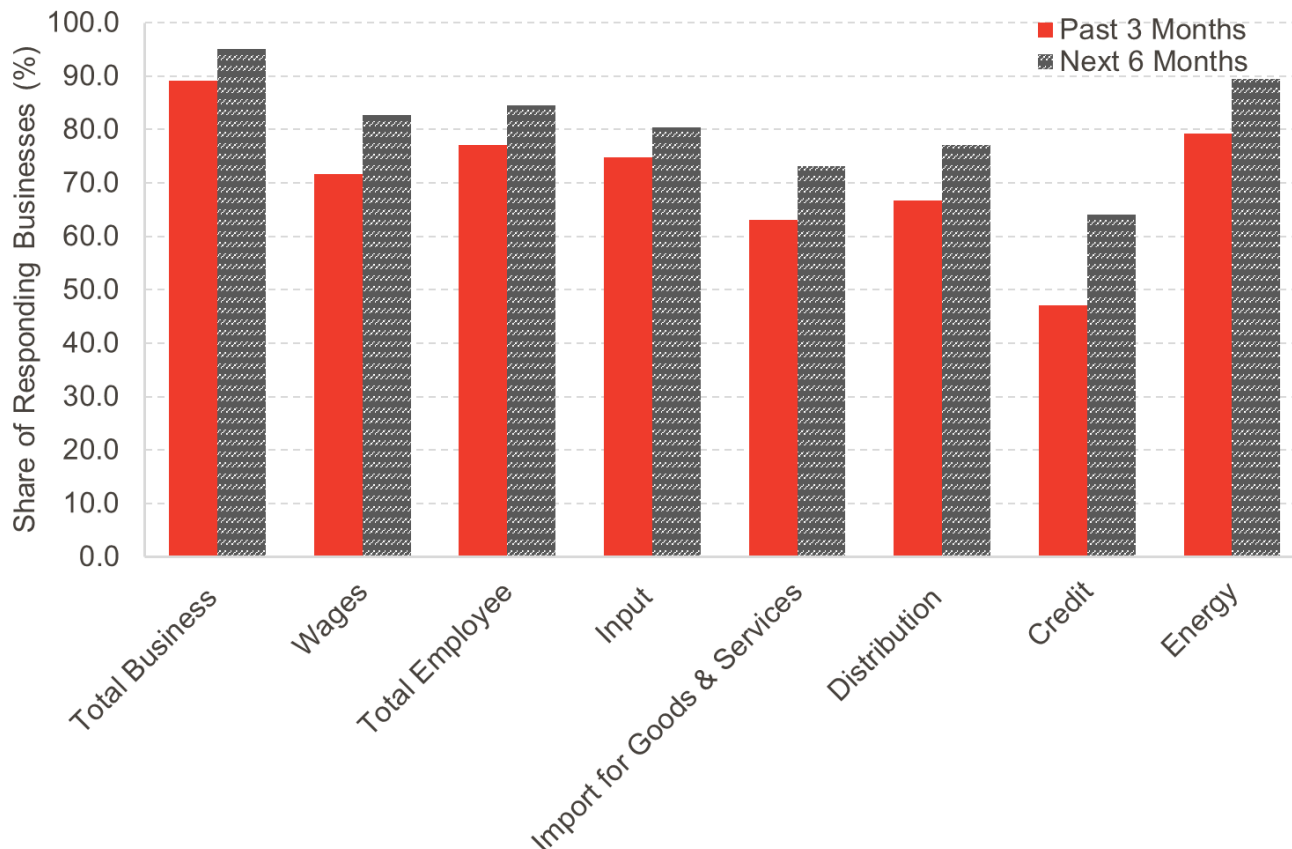
From an economic perspective, this is important because the impact of AI on productivity and business processes will depend less on whether a small number of firms use AI, and more on whether adoption spreads across a large share of the business base. The latest results suggest that this diffusion process is now well underway.

The Scottish Business Monitor will continue to track AI adoption in future waves to monitor whether usage continues to spread across sectors and firm sizes, and to assess how this may affect productivity, investment, and labour demand over time.

## Cost Pressures

Overall costs, particularly energy, have spiked amid international disruption, while some individual cost components show signs of relief.

**Chart 3: Share of businesses assessing costs as 'higher,' in past 3 months and next 6 months, 2026Q1**



Cost pressures have intensified since last quarter with the share of businesses reporting **higher total costs rising from 80.7% to 89.0%** in Q1 2026, and **95.1% of firms now expecting further increases over the next six months**. These pressures are largely driven by disruption stemming from the Iran War:

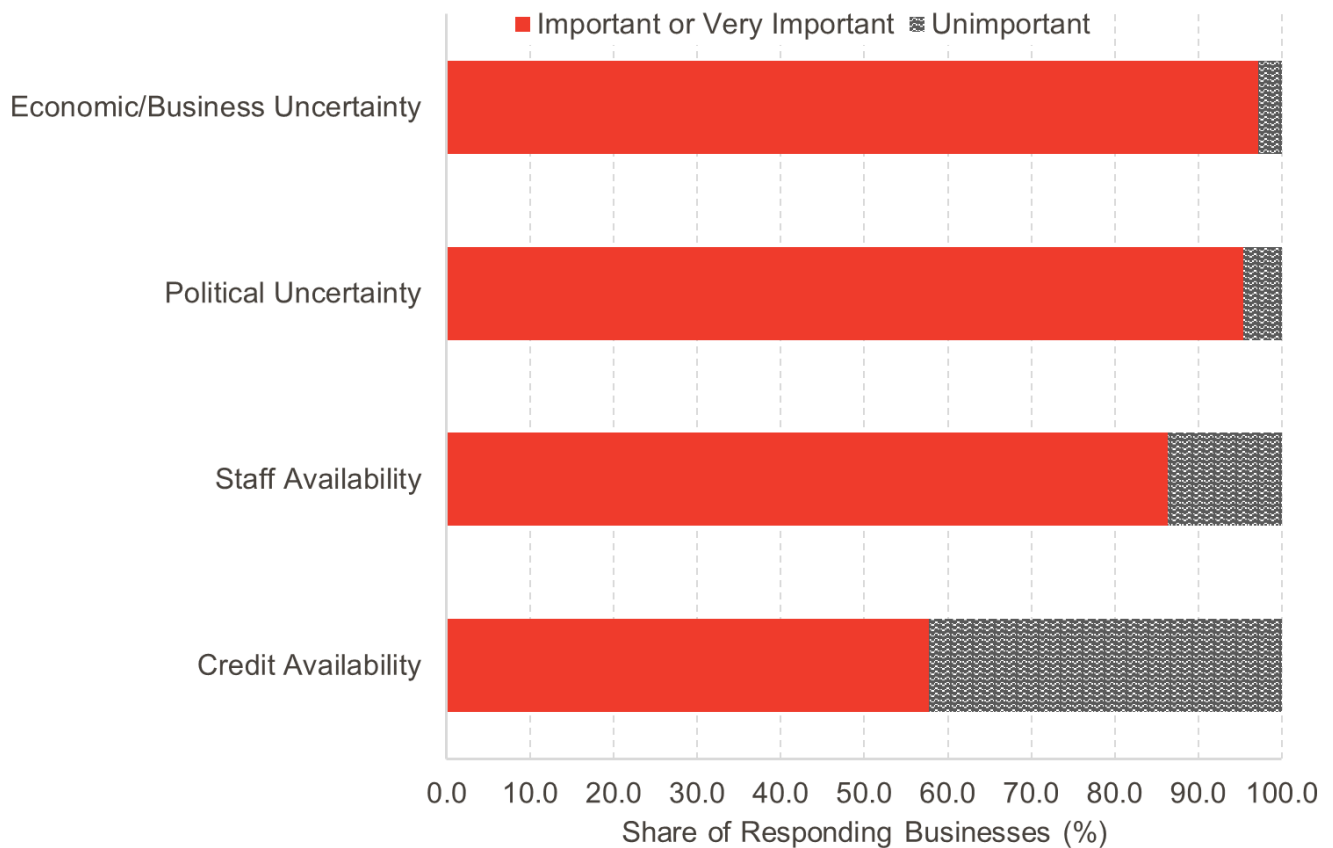
- **Energy costs rose for 79.2% of firms this quarter**, with 89.4% anticipating further increases.
- **Import costs have also climbed, with 63.0% of firms reporting higher costs**, up from around half last quarter, and anticipations for the coming months have similarly risen.
- Distribution costs are similar, with **two-thirds of firms reporting higher costs during the quarter**.

Credit costs also rose with 47.1% of firms reporting higher pressures this quarter, though **forward-looking pressure is notably sharper, with 64.0% expecting increases over the next six months**. This gap suggests firms are bracing for interest rate rises in response to broader inflationary pressures.

**By contrast, employee costs and wages** saw a smaller share of firms report increases in Q1 compared to Q4 last year, with anticipations also easing. While these components still weigh on most businesses, they appear to be alleviating, particularly as the emerging energy shock becomes the primary inflation driver for the remainder of 2026. This confirms the difficult start to 2026, anticipated last quarter, although it should be noted the consequences of the Iran War have amplified the challenge facing Scottish businesses.

# Business Concerns

**Chart 4: Concerns of business over the next 3 months, 2026Q1**



Political uncertainty and credit availability have emerged as growing concerns this quarter, while economic and business uncertainty and staff availability remain broadly stable.

Economic and business uncertainty remains the most widely cited concern, reported as important or very important by 97.2% of firms: unchanged from last quarter. The stability of this figure is itself telling, at near-unanimous levels, there is little room for it to rise further.

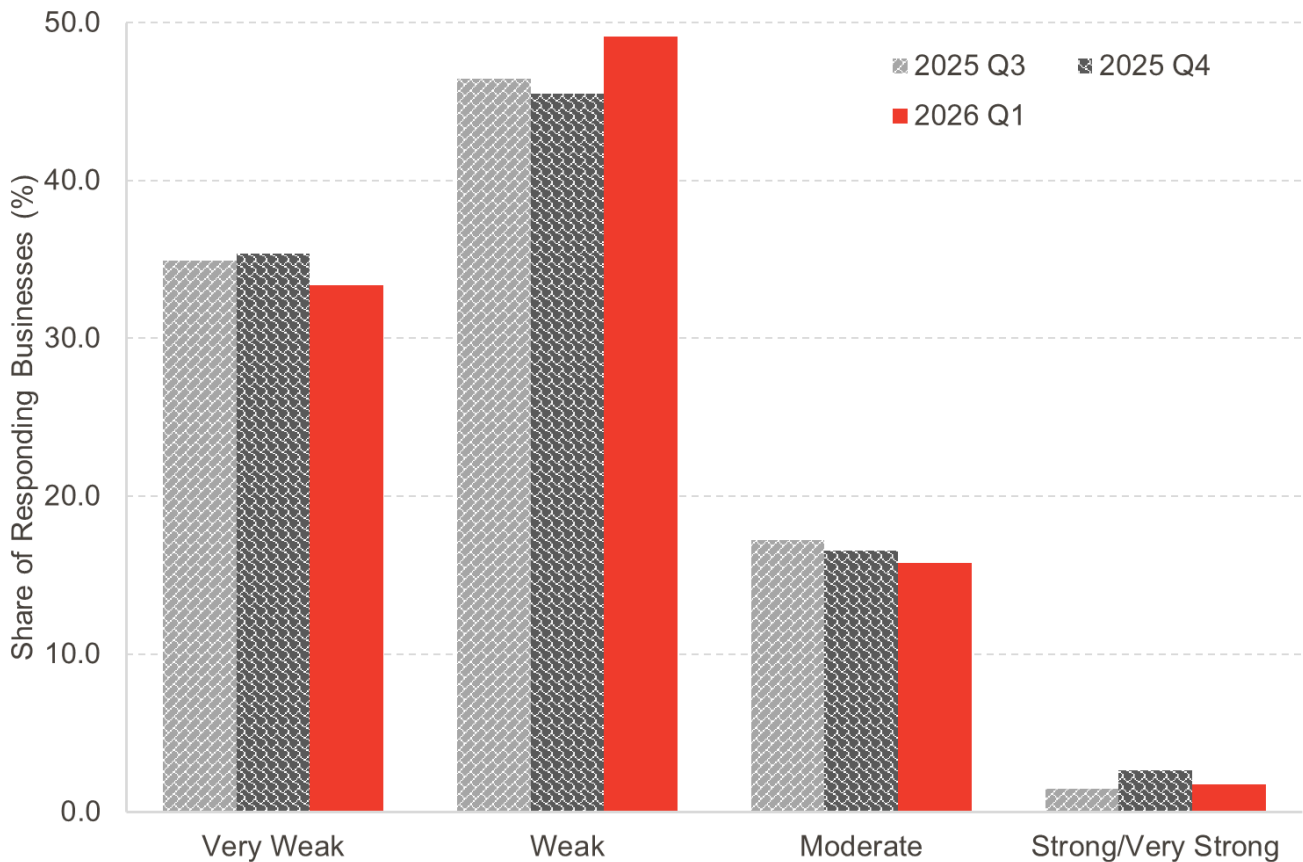
Concern over political uncertainty has intensified, rising 4.3 points to 95.4% of firms rating it as important or very important. Credit availability has also grown as a concern, now cited by 57.7% of firms: likely reflecting forward-looking anxiety around anticipated interest rate rises, as discussed in the cost pressures section of this report.

It is worth noting that businesses are navigating a particularly complex policy environment. While the Iran War is weighing on sentiment, domestic factors are also contributing, including non-domestic rate revaluations and minimum wage increases that came into effect shortly after the survey period closed.

## Economic Growth Outlook

Outlook for growth remains weak, with the share of firms expecting weak growth rising by around 3.6 to 49.3% in Q1 2026.

**Chart 5: Expectations for Economic Growth in the next 12 months, 2025Q3-2026Q1**



The share reporting very weak expectation fell by 2 points, likely reflecting firms shifting into the weak category rather than any improvement in underlying conditions. Combined, weak and very weak demand account for 82.4% of responses, which points to a growth environment that remains deeply subdued.

Moderate expectations held relatively steady at 15.8%, while strong and very strong expectations remained negligible, declining slightly by 0.8 points to 1.8%.

The near-total absence of firms expecting strong growth underlines the scale of the challenge facing businesses, particularly as rising cost pressures, driven by energy and import costs, continue to squeeze margins at a time when revenue conditions offer little relief.