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Economic Commentary

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FOREWORD

Scotland's economic outlook in mid-2026 is defined by a familiar but increasingly complex combination of resilience and uncertainty. The latest data show that the economy continues to grow, marking nine consecutive quarters of expansion, albeit at a modest pace and somewhat behind the UK in the early part of the year.

This edition of the Economic Commentary examines the key forces shaping that outlook. While growth remains positive, it is occurring against a backdrop of ongoing global disruption—not least the effects of geopolitical tensions in the Middle East, which continue to influence energy markets, inflation, and business confidence.

Inflationary pressures have eased somewhat in recent months, but this easing should be treated with caution. The effects of higher energy costs are still feeding through unevenly, with further impacts on households expected over the coming quarters. At the same time, the labour market shows signs of softening, with employment edging down and inactivity increasing slightly. These trends suggest that while the Scottish economy remains resilient by historical standards, it is not immune to the pressures affecting the wider UK and global economy.

Alongside these economic developments, the political landscape has shifted in significant ways. Election results across Scotland, England and Wales point to a more fragmented and fluid political environment, with support moving away from traditional parties and towards a more diverse set of political actors. In Scotland, while the SNP remains the dominant force, the reconfiguration of the opposition benches and the absence of a parliamentary majority point to a more negotiated approach to policymaking in the years ahead.

These changing parliamentary dynamics are likely to have important implications for economic policy and public service delivery. Greater fragmentation in representation may increase the importance of cross-party cooperation, while also shaping the speed and nature of policy decisions. At a time when the public finances remain constrained and difficult trade-offs are unavoidable, the interaction between economic conditions and political realities will be particularly important in determining Scotland's medium-term outlook.

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 FORECASTS

1.0%
2026 forecast

1.1%
2027 forecast

1.2%
2028 forecast

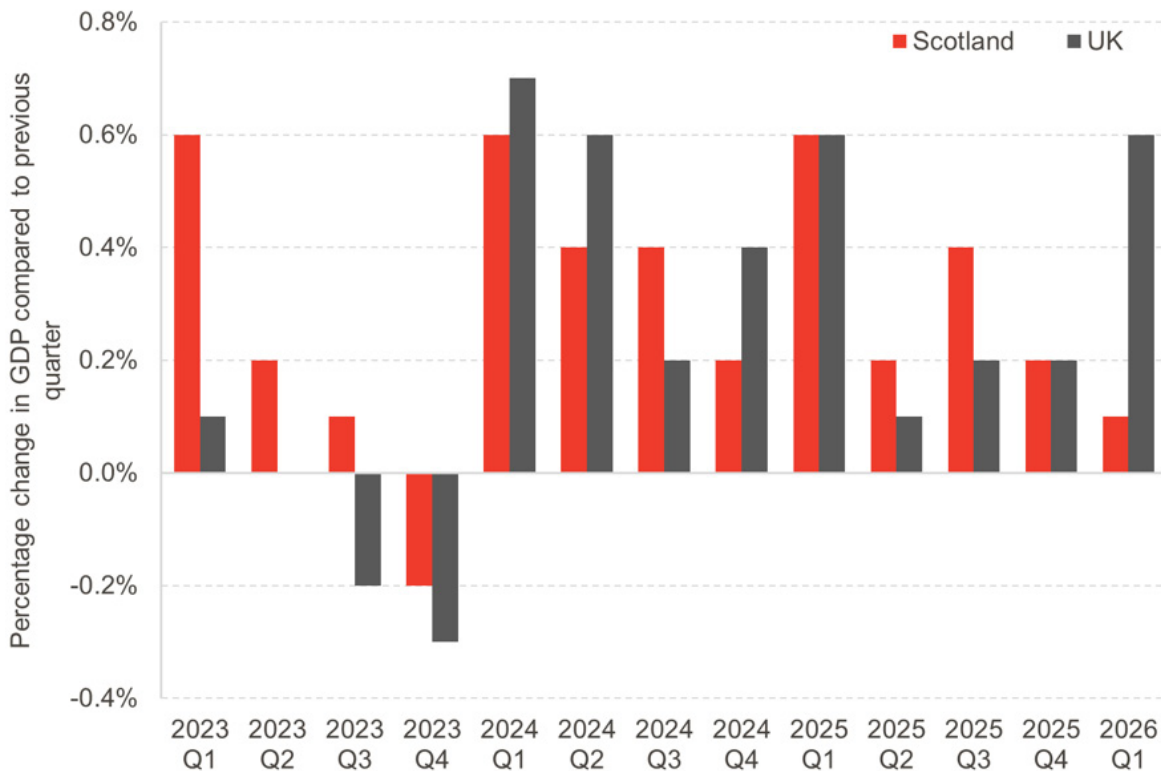
Scottish GDP Growth Forecasts

	2026	2027	2028
FAI June 2026	1.0%	1.1%	1.2%
FAI April 2026	0.9%	1.0%	1.1%
SFC January 2026	1.3%	1.4%	1.5%
OBR March 2026 (UK)	1.1%	1.6%	1.6%

Source: [FAI](#), [SFC](#) and [OBR](#)

The latest available quarterly GDP data reveals positive quarter-on-quarter growth for a 9th consecutive quarter in both Scotland and the UK. Though growth in Scotland is modest compared to the UK in the first quarter of 2026 (driven by a poor February), it is reassuring that the economy is continuing to grow amidst the disruption caused by tensions in the Middle East – although impacts on future quarters remain to be seen.

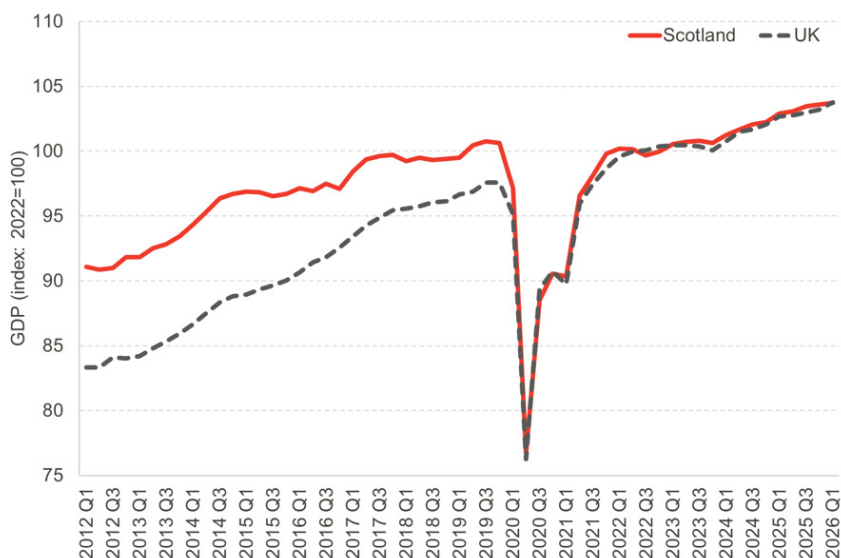
Quarterly GDP Change Scotland vs UK



Source: [ONS](#), [Scottish Government](#)



Scottish and UK Quarterly GDP (2022= 100)



Source: [ONS](#), [Scottish Government](#)

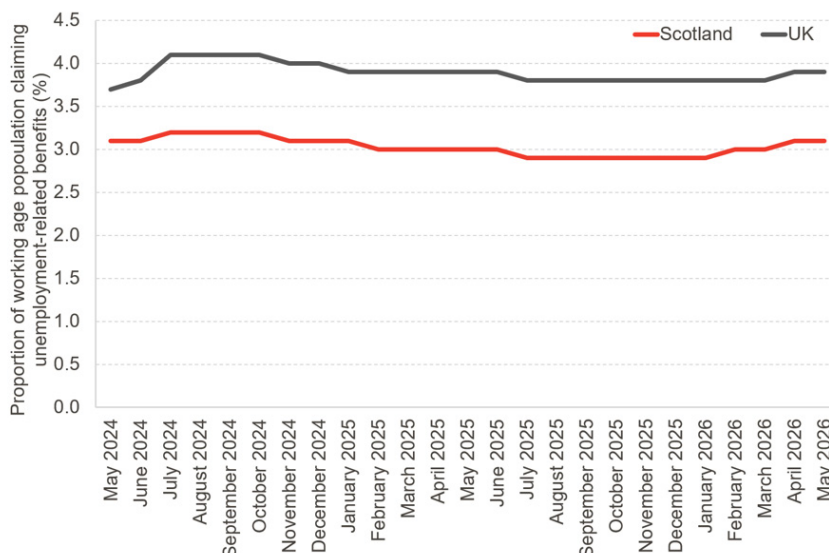
The Scottish economy has continued to demonstrate resilience, with GDP increasing steadily since the disruption caused by the pandemic. Growth has remained positive in recent quarters, contributing to a ninth consecutive quarter of expansion.

Although the UK experienced a somewhat stronger recovery immediately following the pandemic, Scotland has largely kept pace in recent years. By the first quarter of 2026, the two economies were operating at very similar levels relative to their respective pre-pandemic positions, suggesting that Scotland has continued to perform broadly in line with the UK despite ongoing economic uncertainty.

The proportion of the working-age population claiming unemployment-related benefits has grown across Scotland and the UK through the beginning of 2026.

The gap between Scotland and the UK has remained relatively stable since July 2024, with relatively fewer people claiming in Scotland.

Unemployment claimants



Source: [ONS NOMIS](#)

Headline statistics

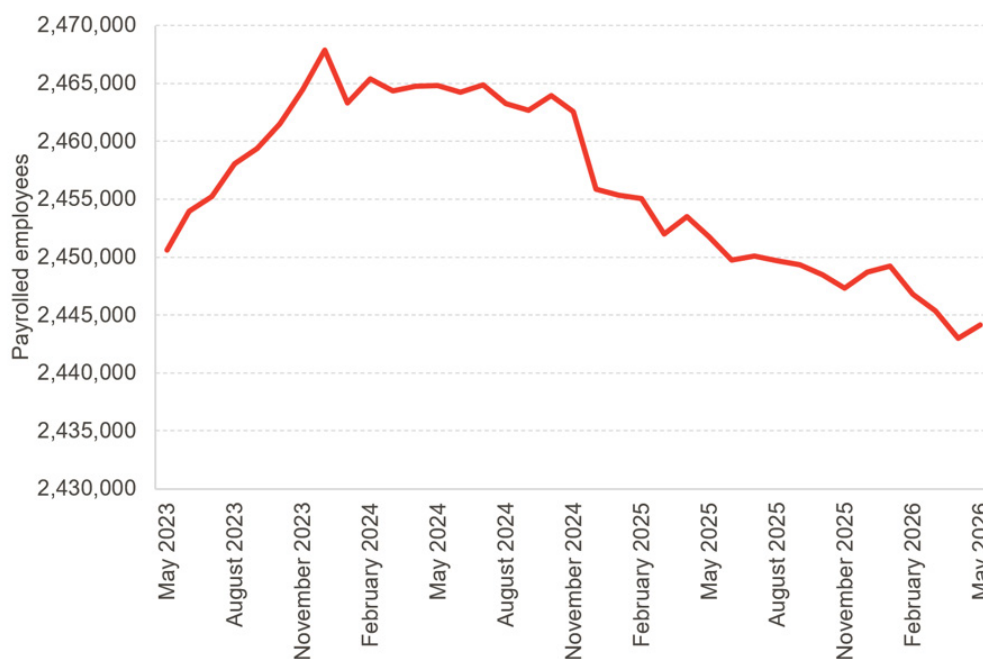
	Employment rate		Economic inactivity rate		Unemployment rate	
	Scotland	UK	Scotland	UK	Scotland	UK
LFS estimate (Q4 2025)	74.8%	75%	22.3%	20.8%	3.8%	5.2%
LFS estimate (Q1 2026)	73.7%	75%	22.7%	20.9%	4.4%	5%

Source: [LFS](#), FAI analysis

The latest labour market indicators point to a modest softening in conditions across both Scotland and the UK. Between Q4 2025 and Q1 2026, Scotland’s employment rate declined slightly, while economic inactivity and unemployment both increased, suggesting some weakening in labour market participation and hiring activity.

Despite this, Scotland continues to record a lower unemployment rate than the UK overall, although economic inactivity remains comparatively higher. Overall, the figures suggest that labour market conditions remain relatively resilient by historical standards, but that both Scotland and the UK have seen some easing in labour demand in recent quarters.

Payrolled employment



Source: [ONS RTI](#)

The number of payrolled employees in Scotland has fallen in recent months to 2,443,010 in April 2026. While the short-term sacking of workers in response to a supply shock – and the resultant hike in operating costs – may be unfeasible for many firms, it is plausible that hiring may be scaled back until cost pressures begin to ease.

Numbers heading into May 2026 showed a slight increase for the first time this year; however, employment figures in the coming months will depend on supply conditions.



Change by sector

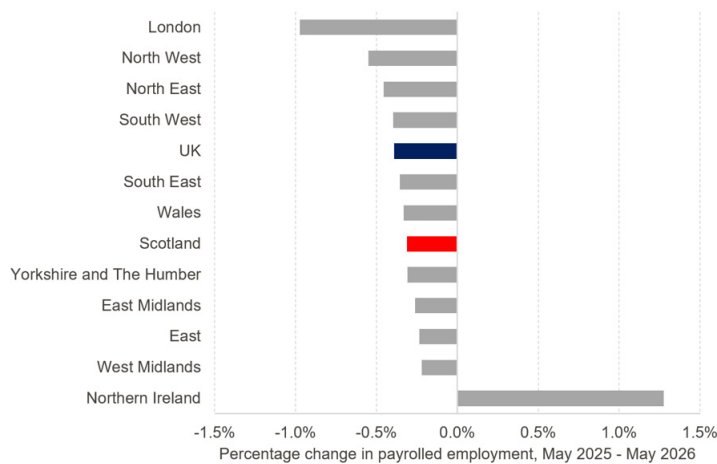
Comparing employment dynamics over the year to April across Scotland and the UK highlights generally similar directions of travel, but greater volatility in Scotland as expansions and contractions tend to be more pronounced than in the UK overall.

In both Scotland and the UK, energy production and supply recorded the strongest increase in payrolled employment, though growth in this sector was markedly stronger at the UK level. This is consistent with activity linked to elevated energy prices and ongoing adjustment in the energy sector. Scotland also recorded relatively strong gains in real estate, finance and insurance, and public administration, suggesting resilience in parts of the service economy.

By contrast, substantial declines continue to be recorded in mining and quarrying, with Scotland experiencing particularly sharp contractions. Employment also fell across a range of consumer-facing sectors, including accommodation and food services and wholesale and retail, likely reflecting continued pressure on household spending and weaker consumer demand, which have weighed on labour demand in discretionary sectors.

Generally, the chart suggests growth remains mainly concentrated in energy-related and higher-value service industries, while consumer-facing and traditional production sectors continue to struggle.

Change by region & nation

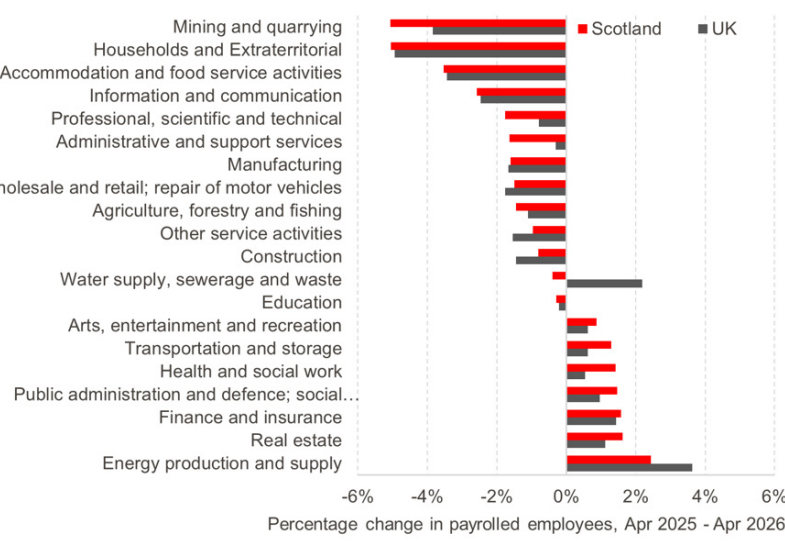


Source: ONS RTI

Over the year to May 2026, payrolled employment declined across almost all regions and nations of the UK, with Northern Ireland the only region to record growth, at just over 1%. London experienced the largest contraction, with payrolled employment falling by around 1%, while most other regions recorded declines of between 0.2% and 0.6%. Scotland's decline was just below the UK average.

The broad-based nature of these declines suggests a general softening in labour market conditions across the UK. However, the sharper fall in London may reflect the capital's greater concentration in sectors that have seen weaker employment growth recently, including professional services and parts of the consumer-facing economy. Given London's size and sectoral composition, changes in hiring activity in these industries can have a more pronounced effect on overall employment. By contrast, Northern Ireland's increase in payrolled employment may partly reflect differences in industrial structure relative to other parts of the UK, including a comparatively larger public sector and lower exposure to some of the sectors experiencing weaker employment trends elsewhere.

Source: ONS RTI

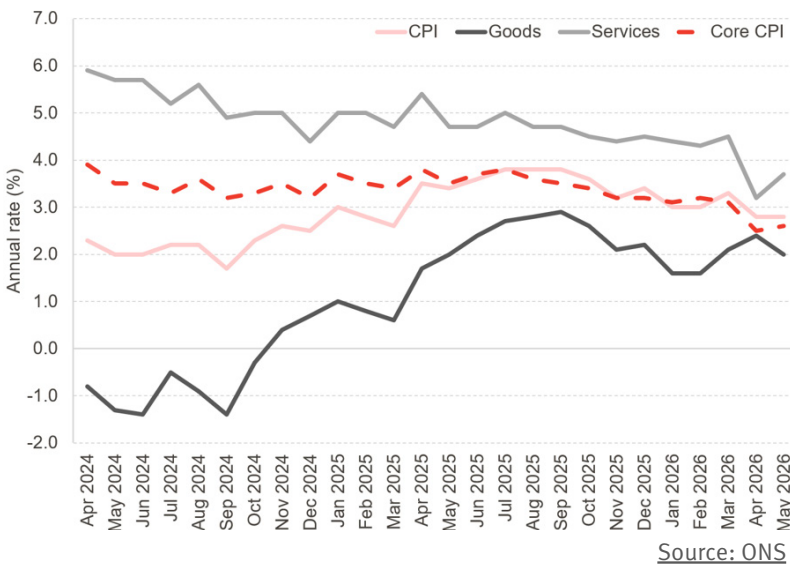


Percentage change in payrolled employees, Apr 2025 - Apr 2026

Source: ONS RTI

INFLATION

Inflation rates in the UK



Source: ONS

The latest official data show CPI inflation holding at 2.8% in May 2026, unchanged from April. CPIH also remained unchanged at 3.0%. Core CPI edged up from 2.5% to 2.6%, while services inflation rose from 3.2% to 3.7% and goods inflation eased from 2.4% to 2.0%. The latest result was driven by higher transport costs, which made the largest upward contribution to the monthly change in the annual rate, partly offset by food and non-alcoholic beverages, which made the largest downward contribution.

Over the latest quarter, headline CPI first rose to 3.3% in March 2026, before falling to 2.8% in April and remaining at 2.8% in May. That easing should be treated with caution, because it partly reflects the timing of household energy prices rather than the full impact of the recent energy shock. The Ofgem energy price cap fell to £1,641 for April-June 2026, down £117 from the previous quarter, helping to reduce household gas and electricity bills. As a result, the latest inflation figures do not yet show the full household gas and electricity effect of the Middle East shock.

The next quarter is likely to show a clearer pass-through of the energy shock to household bills, as the July Ofgem cap incorporates higher wholesale gas prices. From 1st July to 30th September 2026, the cap will rise by 13% to £1,862 for a typical dual-fuel household paying by direct debit. However, recent diplomatic progress between the US and Iran has eased oil prices and points to a possible fading of the shock later in the year, provided that the agreement holds and shipping through the Strait of Hormuz continues to normalise.

ONS data show that transport prices rose by 6.8% in the 12 months to May 2026, up from 4.5% in April, the highest transport inflation rate since December 2022. The main effects behind the increase in the transport annual rate came from air fares, motor fuels, and sea fares.

Average petrol prices rose by 0.6p per litre between April and May to 157.4p per litre, the highest level since November 2022. Overall motor fuel prices were 24.6% higher than a year earlier, up from 23.0% in April and the largest annual increase since September 2022.

The Bank of England's latest assessment is that the energy shock is still feeding through, but with less pressure than it expected in April. At its June meeting, the Monetary Policy Committee voted 7-2 to hold Bank Rate at 3.75%, with two members preferring a rise to 4%.

The Bank noted that some direct effects of the shock, particularly higher fuel prices, had already pushed up CPI inflation, while household gas and electricity bills will be affected more slowly through the Ofgem price cap. It now expects CPI to be a little under 3% in 2026 Q3 and a little over 3.25% in Q4, lower than its April projection because energy prices have fallen back and the May CPI figure was softer than expected.

Even before the latest diplomatic progress became clearer, the Bank had already judged that second-round effects should be more limited than in 2022, as demand is weaker, the labour market is loosening and higher borrowing costs are tightening financial conditions. However, it still warned that the risk of higher prices feeding into wage and price-setting increases the longer energy prices remain elevated.

Overall, the May data suggest that inflationary pressures have not intensified as sharply as feared, but neither have they disappeared. The energy shock is feeding through unevenly: fuel prices and transport costs are already visible in the data, while the effect on household gas and electricity bills will be clearer in the next quarter. Recent diplomatic progress provides some reassurance that the shock could prove temporary, but this depends on energy markets continuing to normalise. For now, the outlook is one of delayed rather than absent pressure, with inflation likely to remain sensitive to developments in energy prices, wage-setting and wider demand conditions over the coming months.



Conflict in the Middle East: the current state of play

As of the end of June 2026, the conflict between Iran, the US and Israel has moved into a fragile diplomatic phase, but it remains unresolved. The House of Commons Library describes the conflict as beginning on 28th February 2026, when the US and Israel launched strikes against Iran, targeting military infrastructure, its nuclear and ballistic missile programme, and security forces including the Islamic Revolutionary Guard Corps. Iran responded by attacking Israel, US bases in the region and sites in neighbouring Middle Eastern states. The House of Commons Library also notes that sea traffic through the Strait of Hormuz largely ended after both Iran and the US established blockades.

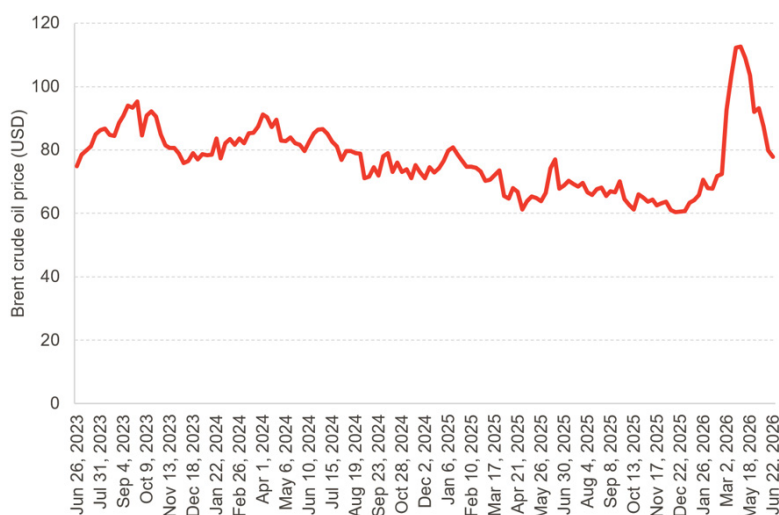
The most important recent development has been the US-Iran memorandum of understanding reached in mid-June. Reuters reported that the agreement provides a framework to end the four-month war and reopen the Strait of Hormuz, although officials warned that traffic would recover gradually rather than return to normal immediately. A separate Reuters summary of the deal said the Strait would start to reopen, the US blockade on Iranian ports would begin to lift, and more difficult issues, including Iran's nuclear programme and sanctions, would be negotiated over the following 60 days.

The economic importance of the conflict continues to come through Hormuz. The House of Commons Library notes that around 20% of global petroleum and 20% of global liquefied natural gas (LNG) normally pass through the strait, with around 3,000 vessels using it each month before the conflict. It also cites World Trade Organization data suggesting that ships carrying crude oil to and from Persian Gulf ports had fallen by 95%, while LNG ships had fallen by 99%, since the conflict began.

Recent data point to partial easing rather than full normalisation. Reuters reported on 22nd June that two crude tankers carrying just under 2 million barrels of oil passed through the strait, but that this remained only a fraction of the pre-war average of 125 vessel crossings per day. Reuters also reported that further tanker movements had resumed, including stranded supertankers and Qatar-linked LNG tankers, but analysts continued to warn that safe passage, insurance confidence and implementation of the US-Iran agreement remain key risks.

Oil prices have responded to the diplomatic progress. Reuters reported that Brent crude settled at \$77.46 in early trading on 23rd June. This is now only around 7% above the pre-war level: Reuters reported that Brent closed at \$72.48 a barrel on 27th February, the day before the conflict began. It also marks a sharp easing from the peak of the crisis, when Brent touched an intraday high of \$126.41 a barrel on 30th April, its highest level since March 2022.

Brent Crude Oil Prices



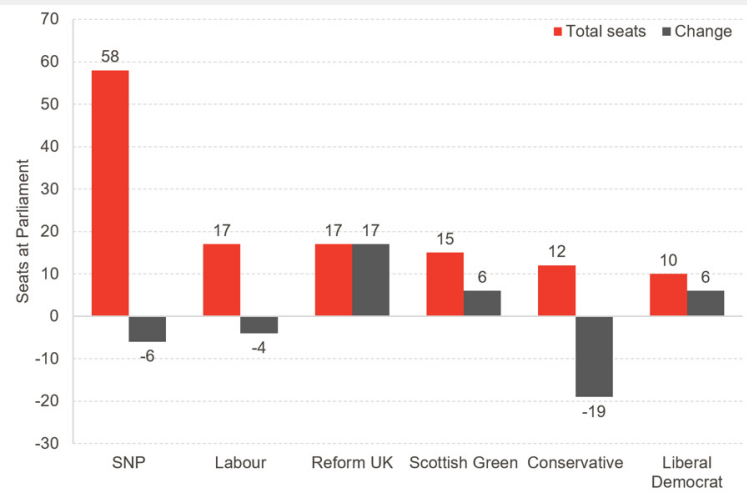
Since April, prices have fallen sharply, returning to around \$80 per barrel by the time of publication. While this suggests that some immediate concerns over energy supply disruption have eased, the volatility observed during the period underlines the ongoing sensitivity of global energy markets to developments in the Middle East.

While prices eased through late May and remain below their peak at the end of March, early June data point to a modest increase. The volatility observed in recent months highlights the ongoing uncertainty surrounding the conflict and suggests that energy markets remain highly sensitive to developments in the region.

ELECTION ANALYSIS

Scottish Parliamentary Election

The Scottish Parliament election produced a familiar headline result, with the SNP remaining by far the largest party at Holyrood. Beneath this continuity, however, the election delivered a significant reshaping of the opposition benches, with substantial gains for Reform UK and losses for the Conservatives, altering the balance of political representation across the Parliament.



Source: BBC, FAI analysis

Despite losing six seats, the SNP retained a dominant position with 58 seats, remaining comfortably ahead of all other parties and preserving its status as the central force in Scottish politics. Labour also experienced a modest decline, losing four seats to finish with 17. Together, these results suggest that while support for the two largest centre-left parties softened somewhat, neither experienced a collapse in representation.

The most notable development was the emergence of Reform UK, which secured 17 seats and entered Holyrood on an equal footing with Labour in terms of parliamentary representation. This gain appears to have come largely at the expense of the Conservatives, who suffered the largest losses of any party, falling 19 seats to just 12. The result points to a substantial reconfiguration of the right-of-centre vote in Scotland, with Reform UK replacing the Conservatives as the principal challenger to the SNP from that side of the political spectrum.

Elsewhere, the Scottish Greens and Liberal Democrats both increased their representation, gaining six seats each. These gains, combined with the SNP's continued dominance, mean that pro-devolution and centre-left parties continue to account for a large majority of seats in Parliament, despite the changing composition of the opposition. Overall, the election suggests continuity in the overall balance of power, but significant change in how opposition to the SNP is represented at Holyrood.

English Local Elections

The English local election results also point to a more fragmented political landscape, with both of the traditional major parties losing ground while smaller parties and challengers made significant gains.

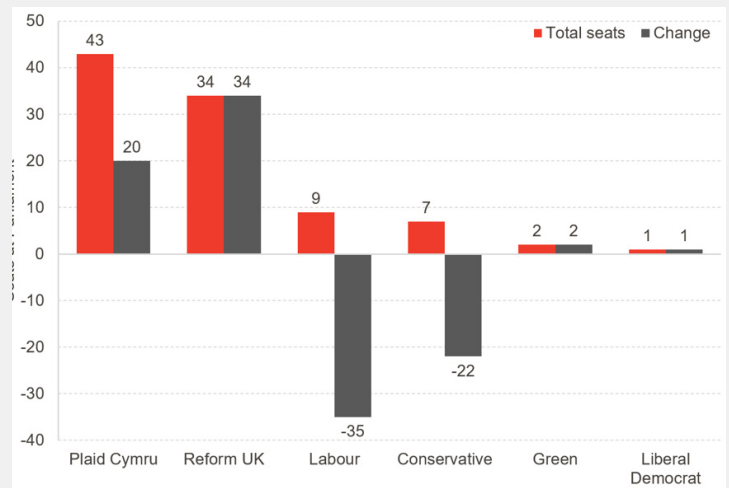
Although Labour remained the largest party in local government, the results suggest that support has become increasingly dispersed across the political spectrum rather than consolidating around a single alternative.

The election proved particularly damaging for Labour, which lost 38 councils, reducing its total to 28. The Conservatives also continued to lose ground, surrendering six councils and falling to nine overall. While both parties experienced setbacks, the scale of Labour's losses was notably larger.

The principal beneficiary was Reform UK, which gained 14 councils and now controls the same number as the Liberal Democrats.

Wales Senedd Election

The Welsh election produced perhaps the most dramatic shift of the three contests. While Plaid Cymru emerged as the largest party with 43 seats, the most striking feature of the result was the collapse in support for both Labour and the Conservatives, alongside a substantial breakthrough for Reform UK. Together, these changes point to a significant realignment of Welsh politics and a departure from the Labour dominance that has characterised much of the devolution era.



Source: BBC, FAI analysis

Plaid Cymru was the principal beneficiary of the election, gaining 20 seats and moving into a clear leadership position within the Senedd. Reform UK also recorded a remarkable result, gaining 34 seats and establishing itself as the second-largest party. By contrast, Labour suffered the largest losses of any party, falling by 35 seats to just nine, while the Conservatives lost 22 seats and were reduced to seven. The scale of these changes suggests that voter dissatisfaction was not confined to a single part of the political spectrum, but instead translated into support for both a centre-left nationalist party and a right-leaning challenger.

Viewed alongside the Scottish and English results, the Welsh election reinforces the broader theme of fragmentation across UK politics.



The Aftermath: What Next for Scotland?

While the SNP once again emerged as the largest party in the Scottish Parliament, the election has nonetheless altered the political landscape in important ways. With 58 seats, the SNP remains seven seats short of an overall majority and faces a Parliament in which five opposition parties have secured double-digit representation. As a result, the next parliamentary term is likely to be characterised by greater negotiation and cooperation across party lines than has been required under majority government.

Shifting dynamics in Holyrood

The election reinforced a broader trend towards political fragmentation. Alongside the SNP's continued dominance, Reform UK recorded a significant breakthrough, while the Scottish Greens and Liberal Democrats also increased their representation. Against a backdrop of declining support for both Labour and the Conservatives, these results suggest that smaller parties may play a more influential role in parliamentary proceedings over the coming session.

Several notable dynamics have emerged from the result. Reform UK's gains appear to have come largely at the expense of the Conservatives, reshaping the balance of the centre-right vote in Scotland. Meanwhile, the strengthened position of the Liberal Democrats and Scottish Greens provides both parties with greater visibility and influence within Parliament. The Greens' performance is particularly noteworthy given the limited number of constituencies they contested, raising questions about their potential role in future elections and the extent to which they can continue to broaden their electoral appeal.

Perhaps the most significant implication of the election concerns the practical operation of government. In the absence of a parliamentary majority, the SNP will need to secure support from other parties to advance legislation and pass budgets. While cooperation with Reform UK or the Conservatives appears unlikely, there may be greater scope for agreement with Labour, the Scottish Greens and the Liberal Democrats on specific policy areas. Both Scottish Greens co-leader Ross Greer and Scottish Liberal Democrat leader Alex Cole-Hamilton have [signalled a willingness to work with the SNP on certain issues](#), providing John Swinney with a number of potential avenues for securing parliamentary support.

For the SNP, the challenge, therefore, will be to build issue-by-issue coalitions while maintaining coherence in its policy programme. The result is likely to be a more negotiated style of government, with parliamentary outcomes increasingly shaped by strategic alignment between parties rather than by a single dominant parliamentary majority.

A slimmed-down cabinet

John Swinney's new cabinet is smaller than the one he led into the election, with only 8 cabinet secretaries – down from 11, meaning the merger of a number of portfolios. Social Justice and Housing are now both under the responsibility Shirley-Anne Sommerville, returning the portfolio to its broad arrangement prior to Màiri McAllan's return to the cabinet in 2025. Rural Affairs have been merged with Energy, and Transport has been merged with the Economy portfolio. The Culture and Gaelic portfolios are now also together with Education, while responsibility for constitutional and external affairs sits directly with the First Minister.

There was however a new portfolio created: Public Service Reform, headed up by Ivan McKee, who was previously Minister for Public Finance. It is much too soon to know exactly how the Public Service Reform (PSR) will co-exist and co-operate with the Deputy First Minister's Finance and Local Government Portfolio. Ivan McKee's [list of responsibilities on the Scottish Government's website](#) still seem somewhat vague, especially compared with Jenny Gilruth's. Will the PSR portfolio act as an arm of Finance, and focus on delivery of a financial strategy laid out by the Deputy First Minister? That would appear to be the movement of travel at the moment, but this is before many of the financial realities collide with the Government's intentions.

There is no doubt that Scotland is facing a pretty difficult set of budgets in the coming years, [as we discussed a few weeks ago](#). While the 2026-27 Budget (and associated Spending Review for 2027-28 and 2028-29) trimmed down the Scottish Government's ambitions according to the funding it was likely to have available, there are still unanswered questions about the plans for delivering efficiencies in the public sector – particularly if there are to be no changes to what is delivered, which the First Minister and the Cabinet Secretary for PSR have implied. We wait to see how the Public Service Reform Strategy (published in June 2025) evolves as the Programme for Government and Draft Budget are published in September and December – which we hope would give clarity to the role PSR is playing in moving Scotland's public services to a more financially sustainable position.

We are of course too close to 2027-28 to introduce any transformative tax legislation that might bring in revenue in that year, and the SNP manifesto showed no appetite for increasing income tax – the Scottish Government's biggest lever for raising additional revenue in this sort of timescale. With that in mind, and in the absence of any unforeseen additional funding from Westminster – which would be imprudent to bank on, especially given the state of the UK's public finances – the adjustment for 2027-28 will have to rest solely on the spending side. The Scottish Government will have to realise those stretching targets on efficiencies pretty quickly if it is to cap job losses in the public sector at the 0.5% a year level it has already announced.



ELECTION ANALYSIS

Uncertain news for financial scrutiny in Parliament

One of the most consequential moments of a Parliamentary session is the allocation and election of conveners to committees. This is especially true for a unicameral legislature like the Scottish Parliament, as the role of committees is even more important for scrutinising legislation.

It was clear there would be a new convener of the Finance Committee, as last session's convener Kenneth Gibson was elected Presiding Officer. Clare Haughey, runner-up in the Presiding Officer election, is the new convener. It would be expected that the SNP would keep the convenership of the Finance Committee – the governing party has held since the dawn of the Scottish Parliament, and it is a principle replicated across the world in Westminster system or Westminster-hybrid systems.

It was however a little disappointing to see the deputy convener being allocated to the governing party as well – even if this is not the first time this has happened, as Labour had both positions from 1999 to 2003, and the SNP from 2011 to 2016. A breadth of points of view in scrutiny and seniority in committees is always important, even more so in the case of a committee overseeing the finances of the Scottish Government in one of the most difficult sessions of since devolution. It will be important that both convener Clare Haughey and deputy convener Alan Brown demonstrate independence regardless of party affiliation – lack of scrutiny may be politically expedient in the short run, but it does no one any favours in the long term.

This is, of course, not the only committee that should be assessing fiscal or financial matters – other policy committees should be considering issues like value for money and opportunity cost as they conduct pre-budget and post-budget scrutiny. Given the cross-party support for shifts to prevention as part of Public Service Reform, as well as the Government getting out of siloed working, the Parliamentary committee system needs to as well.

For example, the Social Justice, Housing and Local Government committee, with Conservative Craig Hoy as Convener, is likely to be scrutinising social security spending closely, along with the consequences of the very difficult outlook for local government settlements and a continued focus on the government's spending commitments on housing. This committee is notable in having an enormous portfolio to cover given the spending in these portfolios.

Scrutiny of real PSR choices, where (say) spending is shifted from one portfolio to another to pursue Prevention for better longer term outcomes, or spending is done in a different way which has poorer short term political wins but much better medium to long-term outcomes (think maybe the way the housing budget is deployed), will require a more mature committee system which understands the imperative to fundamentally change how we deliver public services.

So, therefore it will also be interesting to see what role the PSR Committee itself plays in facilitating this across the committees. Also with an SNP Convener (Bob Doris) and Deputy Convener (Michelle Campbell), this new committee mirrors the new role that Ivan McKee is filling in the Cabinet. Just like the Finance Committee's a role in encouraging other committees to consider financial implications, how will this committee encourage others to walk the talk on PSR?

As touched on above, scrutiny has never been more important than in this session of parliament. Let's see if our parliamentarians rise to the occasion.

For more discussion of the Scottish Parliamentary election results and their implications, as well as analysis of the Welsh Parliamentary election, [click here to listen to our recent podcast](#) featuring Ed Gareth Poole and Guto Ifan of Cardiff University and the Wales Governance Centre, supported by the Nuffield Foundation.

Alternatively, [click here to explore our wider programme of pre- and post-election coverage](#), including manifesto analysis, election commentary and post-election discussion.