# EY ITEM Club Scottish Winter Forecast

March 2025

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# EY ITEM Club Scottish Forecast

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The report is based on data and information available before February 2025. The quarterly EY ITEM Club Scottish report is part of the EY Economics programme which provides knowledge, analysis and insight to help businesses understand the economic environments in which they operate, both in the UK and globally.



# Foreword

**Ally Scott**
EY Scotland Managing Partner
and Corporate Finance Partner
Ernst & Young LLP
LinkedIn

**Sue Dawe**
EY Scotland Head of
Financial Services
Ernst & Young LLP
LinkedIn

Scotland continues to grapple with low productivity and high labour market inactivity. Despite outperforming the UK in 2024, the pronounced slowdown at the end of last year has led to another downward revision of our growth forecast. GDP performance is one indicator that contributes to EY ITEM Club Scotland forecast. Month on month GDP outturn, while important, causes moderate impact on the GVA five-year forecast.

The shared challenge to both public and private sectors is the pressing need to address challenging productivity, labour market and growth trends, and try to turn this into an economic opportunity.

Consumer and business confidence have also taken a hit, reflecting concerns with the economic outlook and looming tax changes. Scotland's proportionately higher population of private, owner-managed businesses means these challenges will be of acute concern – and that's before inheritance tax and associated succession planning is taken into account. Before the last UK Budget, The Business Insights and Conditions Survey (BICS) found 41% of Scottish businesses said they would most likely raise prices to meet any future increases in employment costs and the reality of higher employer NICs is playing out in real time.

Many are watching with interest to see if the mood music around energy policy shifts in the US along with the recent Rosebank court ruling will trigger an uptick in confidence in Scotland's energy sector. With the global sentiment dial shifting even slightly, we could see financing begin to flow somewhat easier into the sector to help solve some of the biggest challenges in our energy transition.

Growth in mortgage lending is forecast to more than double this year as falling interest rates boost housing market activity. This will undoubtedly be welcome news to the construction sector but Scotland's infrastructure requires sustained investment and support to maintain momentum.

Addressing skills shortages and enhancing workforce participation will be essential in revitalising Scotland's labour market. While household incomes are expected to recover, inflationary pressures and cautious business sentiment may dampen investment and, therefore, hiring.

The EY ITEM Club Scotland report continues to underscore the pressing need for strategic interventions across the public and private sectors to address Scotland's low productivity levels and high labour market inactivity.

# Highlights

- Scotland's economy outperformed the UK in 2024. However, the data for the 2024 Q4 is less optimistic, with figures indicating that output was flat across Scotland at the end of last year. Inflation also rose from September to December 2024, prompting the Bank of England to leave interest rates at 4.75% in December. However, concern about faltering economic growth led to the decision to reduce rates to 4.5% in February 2025, and growth prospects for the year are expected to be weaker than previously forecast.

- Across Scotland, the services sectors and construction are driving growth. Consumer-facing services lead economic gains in Q3, with accommodation and food services and arts, entertainment and recreation benefitting from increased consumer spending. However, there was a sharp slowdown in output from these sectors in Q4, suggesting households became more cautious amid growing uncertainty about economic prospects. Among private services, professional services continues to shine posting robust growth at the end of 2024, while the construction sector maintained growth throughout the second half of last year. Forecasts indicate that private services sectors and construction will drive robust GVA growth and maintain above-average growth in the following years.

- Production sectors, on the other hand, are faltering, and data indicates the sectors struggled at the end of 2024. In Q4, production saw a steep fall in output. Within this, manufacturing, mining and quarrying, and utilities all recorded declines. Over the next few years, the shift in fortunes for consumer-facing sectors is most notable, which – after experiencing some of the highest estimated GVA growths in 2024 – are set to lag in 2025 before growth picks up again in 2026.

- Evidence also indicates that the labour market in Scotland is weakening. January survey data indicated a modest fall in employment in Scotland's private sector, mainly driven by employment declines in manufacturing. However, Scottish employers appear to still be posting job adverts for roles they are struggling to fill. With demand easing, joblessness has gradually started to rise. Moreover, with the tax rises and increases to the National Living Wage announced in the UK October Budget, the path for employment growth remains highly uncertain in 2025.

- Business sentiment and consumer confidence appear to have declined (although survey results remain mixed). The declines likely reflect concern following the UK Budget in October 2024, as businesses feel the tax rises would inevitably lead to higher prices and contribute to lower recruitment levels and smaller pay raises. For 2025, Scottish businesses appear to have diverging views; the proportion of businesses expecting their performance to decrease over the next 12 months has fallen slightly, but equally, the proportion of businesses that believe their performance will increase has also declined.

- One of the main risks on the forecast horizon remains the implication of US tariffs. The new US administration has indicated it will impose tariffs on some of its imports. While the UK is unlikely to be targeted, as the US is more likely to focus on countries with which it has a large trade deficit, certain sectors are more vulnerable, including transport equipment and pharmaceutical products, but Scotland's exports of these goods are relatively low compared with the rest of the UK. However, whisky is Scotland's largest export, and the US is its largest export market and could be vulnerable to targeted tariffs.

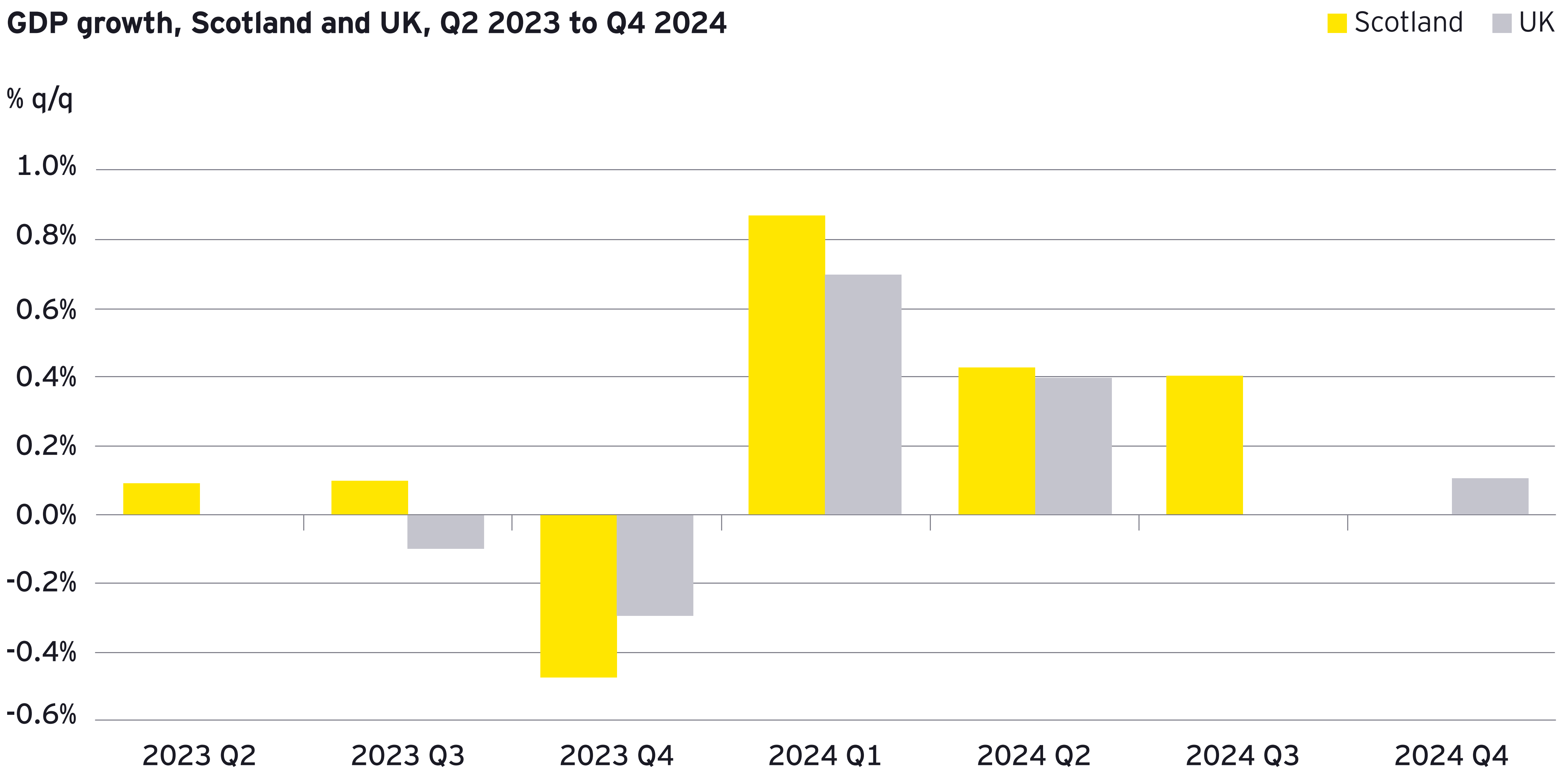
# Latest developments

# Scotland's economic growth stalled at the end of 2024

The latest quarterly data showed Scotland's economy narrowly underperformed the UK in 2024 Q4, reporting that GDP failed to grow in the quarter, following three consecutive quarters of expansion. Scottish GDP increased by 0.4% in Q3. Meanwhile, the UK economy reported no growth in Q3 and grew by just 0.1% in Q4. Over the course of 2024, Scotland's economy looks to have edged UK performance, recording annual GDP growth of 1.1% compared to 0.9% for the UK. While UK and Scottish Q4 results are first estimates and subject to revision, the growth pattern at the end of 2024 is similar, with both the UK and Scotland entering a soft patch at the end of 2024, as businesses contemplated the implications of higher taxes announced in the UK Autumn Budget and rising inflation.

Inflation rose from 1.7% in September to 2.5% by December 2024, mainly because energy prices and weak goods price readings from the end of 2023 were removed from the annual inflation calculation. A further rise of 1.2% in the energy price cap in January will push annual inflation to 3.0% in the near term. The evidence of rising inflation meant that the Bank of England left interest rates at 4.75% in December, but concern about faltering economic growth led to the decision to reduce rates to 4.5% in February 2025.

**GDP growth, Scotland and UK, Q2 2023 to Q4 2024**




Source: Scottish Government/ONS

# Services sectors and construction driving growth as production sectors falter

Scotland's GDP growth in the second half of 2024 was mainly driven by expansion in services sectors and construction activity, while production sector activity faltered and showed decline in Q4. Performance was buoyant across many parts of the services sector, but the highest growth rates in Q3 were reported in largely consumer-facing sectors. These include accommodation and food services (3.6%) and arts, entertainment and recreation (3.1%), with these sectors benefitting from sustained growth in consumer spending in Scotland. Consumer spending was the largest contributor to GDP growth across the first three quarters of 2024, eclipsing the contribution from government spending and investment. However, the sharp slowdown in output from the consumer sectors in Q4 is notable, suggesting households became more cautious about their spending amid growing uncertainty about economic prospects. Output declined by 1.3% in accommodation and food and fell by 0.9% in the arts, entertainment and recreation sector. Despite growth in household spending across the year, the performance of the retail and wholesale sector continued to disappoint in 2024, with output declining by 0.5% in Q4 and by 1.3% for the year. This followed decline of 2.1% in 2023 and in 2024 output from the sector was 6.4% smaller than recorded in 2019.

Against weakening consumer sentiment, the professional, scientific and technical services sector continues to shine, recording a further 2.3% expansion in Q4. Output from the sector is 3.4% larger than a year previous and over 18% greater than the 2019 average. The sector is not only benefitting from strong domestic demand but also from international demand, as the export of UK professional services grew by 0.8% in the year to 2024 Q3. Only the information and communication sector has outperformed professional services, with output over 43% larger in 2024 than the 2019 average. However, its growth rate has slowed consecutively in recent quarters, and output declined by 1.0% in 2024 Q4 compared with growth of 2.4% in Q1.

The recent data also confirms that the production sector struggled at the end of 2024. Having recorded no growth in Q3, production output fell by 1.1% in Q4. Within this, manufacturing output fell by 1.8% compared with the previous quarter, and output has declined by 1.3% over the year. Elsewhere, the mining and quarrying and electricity and gas supply sectors also recorded annual declines in output, with only the water supply and waste management sector expanding over the course of 2024.

The construction sector also helped drive growth at the end of 2024, rising 0.5% in Q4, following growth of 0.7% in Q3. However, the industry has struggled to maintain momentum and periods of growth over the last year have been followed by periods of contraction. This erratic pattern means that output from the Scottish construction sector in 2024 was almost identical to the level recorded the year previous.

UK bank-to-business lending growth is expected to increase from 2.9% in 2024 to 4.5% in 2025 – the highest rate since 2020 – and 5.6% in 2026 as borrowing rates continue to fall.

UK mortgage lending growth is forecast to more than double this year – up from 1.5% (net) in 2024 to 3.1% (net) in 2025 – as falling interest rates and rising consumer confidence boost housing market activity. However, with rising house prices and high mortgage rates persisting, mortgage lending growth is expected to be steady thereafter, with growth forecast at 3.2% (net) in 2026.

Overall, economic recovery has been slower than expected, but growth is set to build steadily over the next two years. This will feed through to the banking sector as interest rates continue to fall – as seen in February's Bank Rate decision – and appetite to borrow strengthens over time. As a result, total UK bank lending is forecast to rise to 3.7% (net) this year (up from 2.3% in 2024) and 4.1% (net) in 2026 and 4.3% (net) in 2027. Demand for consumer credit is expected to remain steady, with growth of 5.8% in 2025 (down from 6.4% in 2024) and 6.8% in 2026.

Following no growth in UK mortgage lending in 2023 (0% net), interest rate cuts, falling inflation and real income growth, boosted housing market activity in the second half of 2024. This resulted in modest mortgage lending growth of 1.5% (net) in 2024. With further, albeit gradual, interest rate cuts predicted this year, consumer confidence and appetite to borrow is also expected to grow, and the EY ITEM Club forecasts UK mortgage lending growth to more than double to 3.1% (net) in 2025.

# Labour market

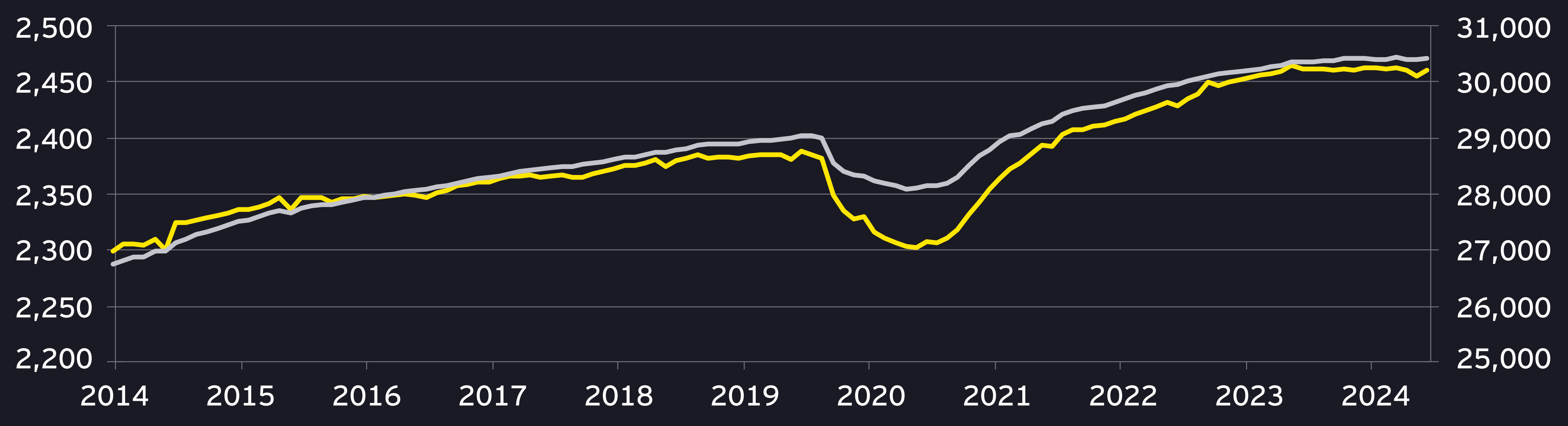
Evidence of weakening labour demand in Scotland is mounting. Recent survey results from the RBS January 2025 Scotland Growth Tracker showed a modest fall in employment in Scotland's private sector following 22 months of consecutive growth. The reported decline was driven primarily by a downturn in manufacturing, but job creation in service firms also continued to cool. While business surveys may be overly sensitive to business sentiment and changes to government policy, official statistics show PAYE payroll employment was 2.46 million in January 2025, a modest increase from the previous month. However, payroll employees fell in both November and December and were unchanged across most of 2024. A similar trend is evident in the UK, but the rate of decline in recent periods appears more pronounced in Scotland.

Data on job adverts provides another indication of the health of the labour market and a gauge of employer demand. Unfortunately, the ONS has discontinued the publication of the previous online job adverts dataset and replaced it with an alternative series that is not comparable with previous statistics (although it does provide a time series back to January 2018). Data reliability warnings aside, the new data indicates a similar number of job adverts for Scotland in November 2024 as the previous year, with the decline in the month consistent with seasonal patterns. Comparable data for the UK showed a comparatively lower number of job adverts in November 2024, with the level down 6.6% on November 2023. Scottish employers may still be posting job adverts for roles they struggle to fill. Findings from the ONS Scottish BICS show that a fifth of businesses continued to report worker shortages in January 2025, still a considerable proportion but down on the 25% reported in October 2024. Worker shortages are most acute in administrative and support service activities, health and social work, professional, scientific and technical activities and construction.

With demand easing, joblessness has gradually started to climb, with the unemployment rate rising from 3.5% in the July-September period to 3.9% in October-December. However, the rate remains below the UK average of 4.5%. While the hiring rate among businesses is slowing, there is little evidence that firms are laying off staff, and estimates of redundancies remain low in Scotland. The number of redundancy notifications stood at around 1,300 in December 2024, half the number reported in December 2023. The comparable figure for Great Britain shows slight growth over that period, although the figures remain around normal levels.

Cooling labour demand appears to be filtering through to salary growth in Scotland, with the latest PAYE earnings data suggesting that median annual pay growth slowed to 5.2% in the year to January 2025, remaining below the UK at 5.7% and a marked slowdown on rates of over 7% reported in the autumn.

**PAYE employees, UK and Scotland, 2014 to 2025**




Source: ONS

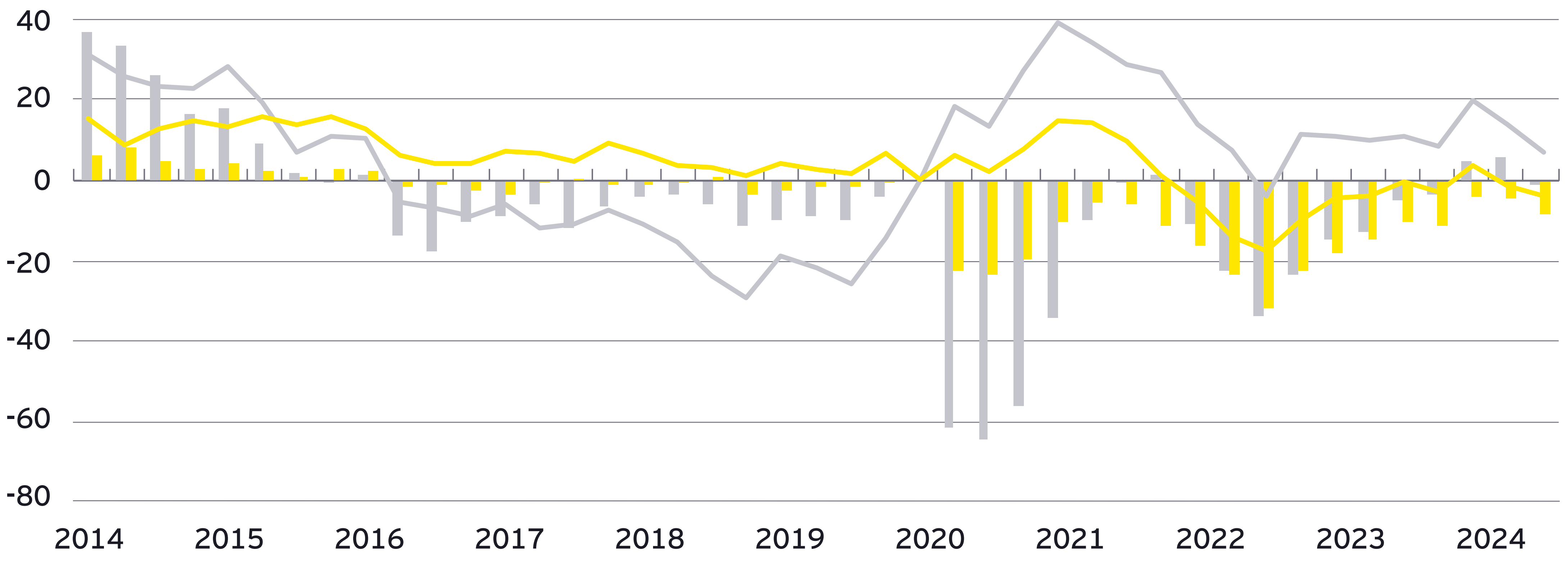
# Consumer and business confidence affected by concerns over the economy and rising taxes

In 2024 Q4, the Composite Consumer Sentiment Indicator fell to -4.9, its lowest level since 2024 Q1. All five sentiment indicators covering current and expected economic performance, household finances and attitudes to spending declined over the quarter. It is likely that this reflects concerns about October's UK Budget and the vocal response from businesses, and that in their opinion, the tax rises would inevitably lead to higher prices, lower recruitment levels and smaller pay raises. This assertion seems to be supported by the relative decline of consumer responses around the economy's current performance and its prospects for the year ahead, compared with their concerns about household finances, which also fell, but to a lesser degree.

Business sentiment also declined, although the readings across surveys for Scotland are somewhat mixed. The Scotland Growth Tracker index recorded a value of 46.9 in December 2024, down from 51.1 in the previous month and a more significant decline than observed across the UK as a whole. An index reading below 50 indicates a contraction in activity in Scotland, and it was the first reported decline in a year. However, the Lloyds Bank Business Barometer for January 2025, which uses a different measure and is timelier, recorded confidence at 42 in Scotland, above the UK average of 37 (although Scotland's score dropped by two points from December 2024).

Scottish businesses appear to have divergent views on their prospects for the coming year. The ONS Scottish Business Insights and Conditions Survey (BICS) for February found that 28.9% of businesses thought their business performance would increase over the next 12 months, down from 33.0% reported in January. At the same time, a smaller proportion of businesses expect performance to decrease, reported by 12.7% of businesses in February, down slightly from 14.0% the month previous. The Scottish BICS also reported that the most significant concern for businesses remains falling demand for goods and services, reported by 14.6% of businesses, down slightly on the proportion reported in October (16.9%). However, following the UK Budget, taxation is now the second greatest concern, cited by 12.4% of businesses, and was more of an issue for small and medium-sized businesses. Taxation was the principal concern for 12.9% of small to medium-sized businesses, compared with 8.2% of large businesses.

**Consumer indicator scores and expectations, Scotland, 2014 to 2024**




Source: Scottish Government

# Economic outlook

## Growth prospects for this year are weaker than previously forecast, but momentum should return

Scottish GVA growth of 1.1% is a significant improvement on the 0.5% recorded in 2023, and we think that the lower activity at the end of 2024 was a soft patch rather than a fundamental change in underlying conditions. Household incomes continued to recover and strengthen in 2024, which is expected to support stronger consumer spending growth in 2025. However, we think inflation will be slightly higher for longer, affecting spending, while businesses' caution will likely hamper investment. The loss of momentum at the end of the year will also take time to unwind. These factors dampen prospects for this year, and we have revised our forecast as a result. We now expect GVA growth of 0.9% in 2025, slightly below the estimate for 2024 and the 1% growth expected at the UK level this year.

Inflation will likely stay above the 2% target for most of this year, averaging 2.8% over 2025, with domestic inflation pressures likely to be slower to ease. While the continued loosening of the labour market should lead to lower pay inflation, the rise in employers' National Insurance Contributions (NICs) – which come into force in April 2025 – will mean employers continue to face elevated labour costs even as pay growth slows. The level of joblessness may rise slightly in the near term in 2025, but the unemployment rate is expected to decline gradually thereafter.

Despite weakening real income growth (as pay growth slows and inflation rises), consumer consumption will continue to drive growth as less consumer caution sees the saving ratio fall. We think consumer spending growth will pick up to 1.6%, supporting GVA growth of 1.5% and 1.3% in 2026 and 2027, respectively. Scottish growth is expected to follow a similar pattern to the UK, but the outlook is slightly weaker, with UK GVA forecast to expand by 1.7% in 2026 and 1.5% in 2027, respectively. The somewhat softer outlook for Scotland is mainly attributable to its industrial profile, with a higher dependence on sectors that are likely to show slower growth, notably manufacturing and the public sector.

Global growth should be stable in 2025; however, the US administration will likely impose some tariffs. It is unlikely that the UK will be singled out as a trading partner that should face exceptionally high tariff rates. However, growing uncertainty appears to have affected business and consumer sentiment in Scotland. The global outlook is highly uncertain, given potential changes to international trade policy and broader geopolitical tensions. Risks to the forecast, even for the short term, remain high.

**Key economic indicator outlook, Scotland, 2020 to 2027, % year-on-year (unless otherwise stated)**

| | GVA | Personal disposable income | Consumers' expenditure | Population 000s | Employment 000s | Unemployment rate % | Migration aged 16–64 (000s) |
|---|---|---|---|---|---|---|---|
| **2020** | -12.0 | -0.2 | -12.8 | 5,413 | 2,755 | 4.5 | 12.2 |
| **2021** | 8.9 | 0.6 | 7.9 | 5,418 | 2,781 | 4.3 | 15.6 |
| **2022** | 5.0 | -2.7 | 7.0 | 5,447 | 2,810 | 3.4 | 41.4 |
| **2023** | 0.5 | 0.4 | 0.3 | 5,490 | 2,867 | 4.1 | 46.7 |
| **2024** | 1.1 | 3.6 | 0.5 | 5,554 | 2,909 | 3.9 | 55.7 |
| **2025** | 0.9 | 1.8 | 1.2 | 5,586 | 2,919 | 4.1 | 29.3 |
| **2026** | 1.5 | 0.2 | 1.6 | 5,618 | 2,938 | 4.0 | 37.2 |
| **2027** | 1.3 | 0.8 | 1.3 | 5,638 | 2,948 | 3.9 | 31.5 |

Source: EY ITEM Club. Note: GVA is in chain-linked 2022 prices. Personal disposable income and consumer expenditure are also 2022 prices. Unemployment rate is the International Labour Organisation (ILO) unemployment rate using Labour Force Survey data.

## Consumer-facing sectors will likely suffer this year, but growth will pick up as spending begins to rise

The caution that hit consumers and their spending at the end of 2024 is expected to drag through into this year, which affects our forecasts for the consumer-facing sectors, which are weaker than our previous forecast. Most notable is the shift in fortune for the arts, entertainment and recreation sector, which, after experiencing the highest estimated GVA growth in 2024, is set to record the largest contraction, with a 7% decline anticipated this year. However, as spending recovers, growth will return, and the sector is expected to exceed the economy-wide average in both 2026 and 2027. A similar outcome is anticipated for the accommodation and food sector. However, here, the swing between growth last year and the forecast decline for 2025 is less stark and is expected to bounce back in the following years. Meanwhile, we expect wholesale and retail trade to report growth in 2025 after a disappointing 2024. However, the growth of 0.6% is still below the economy-wide average, and output from the sector is not expected to recover to pre-COVID-19 pandemic levels in the forecast horizon.

With weaker consumer spending forecast for this year, the bulk of growth is set to be provided by a few key sectors. In the services sector, information and communication should shrug off the weakness recorded at the end of 2024 and return GVA growth of 2.6%, somewhat down on the post-COVID-19 pandemic highs the sector has enjoyed in recent years but still leading growth among private services sectors. Close behind is expected to be professional, scientific and technical services, which is anticipated to maintain its strong and steady growth path. Both sectors should continue to enjoy growth from domestic and global opportunities amid growing demand for AI and the continued growth of UK service exports. However, demand for often lower-value administrative and support services is expected to remain weak, and output is expected to grow only marginally in 2025 after declining last year.

Alongside growth in key private sectors, construction should bolster Scotland's overall growth. While the sector has struggled to maintain momentum in recent years, there is a growing pipeline of infrastructure projects that should start to feed through to growth this year, and the delays that have plagued Scottish housebuilders also appear to be clearing, with housing delivery up at the end of 2024. These factors should drive GVA growth of 2.2% in 2025 and maintain above-average growth in the following years.

However, the risk of returning inflationary pressures filtering through to building materials, alongside higher employment costs, could hamper its progress.

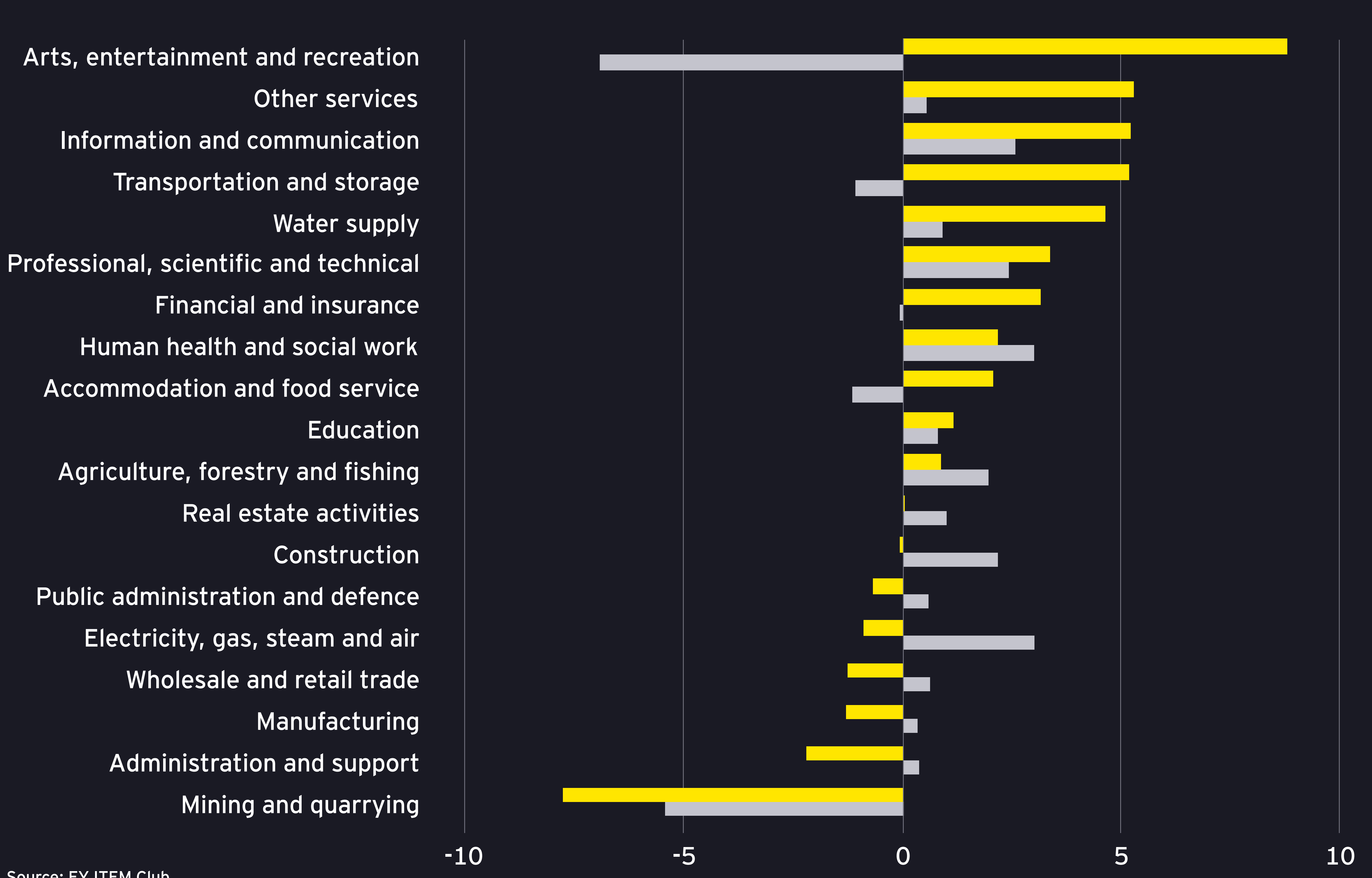
Human health is the other key sector expected to drive output growth this year. The sector is prominent in Scotland and accounts for 11% of the total GVA. Following the £2 billion increase in health and social care spending announced in the December Scottish Budget, we have upgraded our forecast and now expect the sector to expand by 3% this year, after growth of 2.2% in 2024. Despite funding commitments and growing demand for health services, we think that this pace of GVA growth is unlikely to be maintained as fiscal pressures tighten. Because of the sector's scale, below-average growth of 1.5% will still contribute significantly to overall economic growth.

While not as significant in sheer scale, Scotland's public administration and defence sector accounts for 7% of Scottish GVA compared with 5% in the UK. Following an estimated decline of 0.7% in 2024, we expect output to rise by 0.6% in 2025, a slight improvement compared with our previous forecast and reflecting the higher funding from Westminster announced in the Autumn Budget. However, we continue to expect growth to be considerably weaker in the future than in the recent past as fiscal budgets are squeezed. Prospects are somewhat better for the education sector, which also supports 7% of Scottish output. We think the sector's GVA will expand by 0.8% this year but ease to 0.6% in 2026.

Another significant sector for Scotland is the financial and insurance sector, which supported 9% of the total output in 2024. The sector grew by an estimated 3.1% in 2024, bucking the recent trend of decline (GVA fell by 2.3% and 1.1% in 2022 and 2023, respectively). However, much of last year's growth came in the first quarter, with only slow growth reported over the rest of the year. And according to monthly data, output from the sector was smaller in November 2024 than in March 2024. We believe 2025 will be a challenging year, with growth close to zero. Prospects are better for the following years, though we continue to expect competition with other regional financial centres both in the UK and internationally to increase in the coming years, limiting growth to around 1% per year in 2026 and 2027 and slightly lagging the UK average.

Scotland's manufacturing sector accounts for a similar proportion of GVA as the finance sector, and it has experienced similarly mixed fortunes in the recent past. However, the last two years have been marked by decline, as output shrunk by 4.1% in 2023 and an estimated 1.3% last year. This is in sharp contrast to the sector's performance in the wider UK. Though far from outstanding, the UK manufacturing sector recorded growth of 1.0% in 2023, while output declined by 0.7% 2024, a smaller decline than observed in Scotland. The main explanation for the difference is found in the subsector profile, with Scotland's significant food and drink sector – mainly attributable to whisky – declining by 5.6% and 4.6% in 2023 and 2024, respectively. We expect the food and drink sector to return to growth this year, which helps support the overall weak growth rate for the broader manufacturing sector of just 0.3%. However, this should improve in 2026 as the contributions from other subsectors pick up. Notably, the contribution from typically higher-value manufacturing, including transport equipment and electrical and instrument engineering, is expected to expand to meet growing domestic and international demand.

**GVA growth by sector, Scotland, 2024 and 2025, % year-on-year**




Source: EY ITEM Club

# Employment outlook is weaker and more uncertain

With the softer economic outlook for 2025, the path for employment growth this year is less certain. While pay growth may continue to ease, the upcoming increases to employers' NICs are likely to increase labour costs. The Institute for Fiscal Studies estimates that, on average, the changes in employers' NICs will push up the cost of an employee by £900 per year, and growth in businesses' labour costs is unlikely to slow much over 2025. While firms may absorb some of the increased cost, the Bank of England's Decision Maker Panel survey reports that UK businesses' most likely response will be to lay off workers and raise prices. However, ahead of the UK Budget in September 2024, according to the Scottish BICS, Scottish businesses were most likely to report that they would increase their prices (41%) or absorb within profit margins (35%) any future increases in employment costs, and only 16% said they would reduce headcount. The scale of increases in the Budget was likely higher than many businesses anticipated, and their plans may have subsequently changed. In any case, the BICS survey shows that in January 2025, 11.4% of businesses expected employee numbers to increase compared with 14.5% in September.

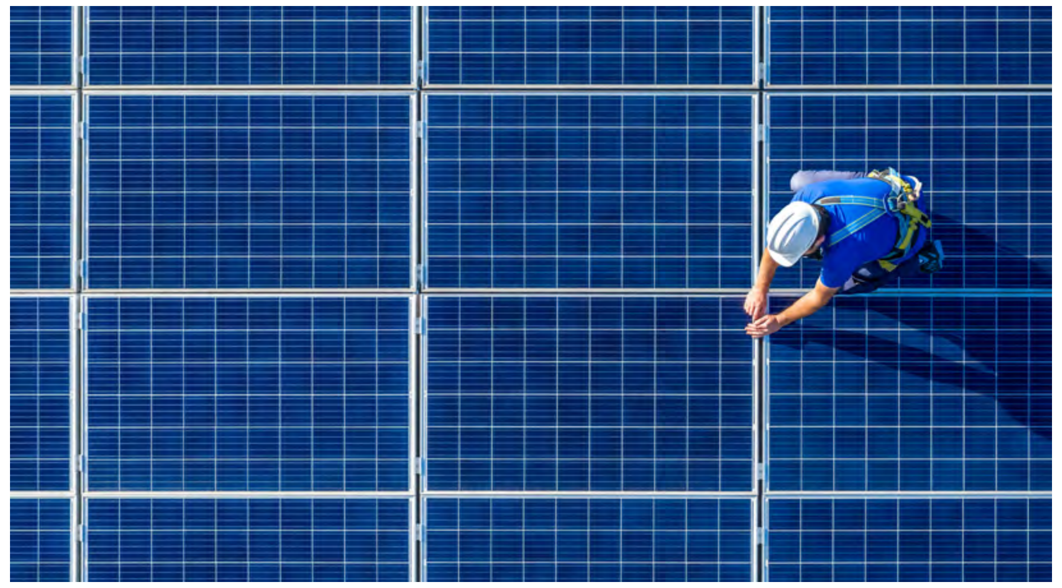
Exactly how firms will respond is highly uncertain. While we have lowered our forecast for employment growth to just 0.3% for 2025, we cannot rule out weaker employment growth and potentially a larger rise in unemployment if firms opt to reduce headcount sharply in response to higher costs. The weaker outlook for this year is most notable among mainly consumer-facing services, with hiring set to be scaled back because of lower forecast demand. Across these sectors, we expect no growth in wholesale and retail jobs this year, a small decline in arts, entertainment and recreation, and relatively muted growth in accommodation and food. However, the downside risk to the outlook for these sectors is greater, as they also typically have relatively higher concentrations of lower-paid staff. This means that they are more vulnerable to the higher NICs, as the changes involve reducing the threshold at which firms start paying tax and the 6.7% increase in April in the National Living Wage. In addition, changes to employment rights will also likely increase labour costs, and it is these same sectors (alongside social care) that appear more vulnerable to changes, as proposed measures include the ban on zero-hour contracts and the requirement to provide statutory probation periods.

Longer-term employment growth in Scotland is also expected to be weaker than seen in recent periods, particularly compared with the post-COVID-19 pandemic average, when employment increased by 1.4% between 2021 and 2024. Over the 2025 to 2029 period, we expect the Scottish economy to create around 62,000 net new jobs, equivalent to an average annual growth of 0.4%. Productivity growth will make a more significant contribution to growth, with output per worker expected to increase by an average of 0.8% per year over the same period. This outcome partly reflects the shifting sectoral profile of growth, with faster growth in some sectors that tend to be more productive, such as professional services and information and communication. However, we also assume that productivity growth will be stronger economy wide. This assumption reflects technological shifts and the use of tools, such as AI, to perform routine tasks more efficiently. This is also symptomatic of Scotland's weakening demographic outlook in the long term. With a very low working-age population growth of 0.2% per year expected over the period, the scope for increases to Scotland's labour supply and jobs growth is limited.

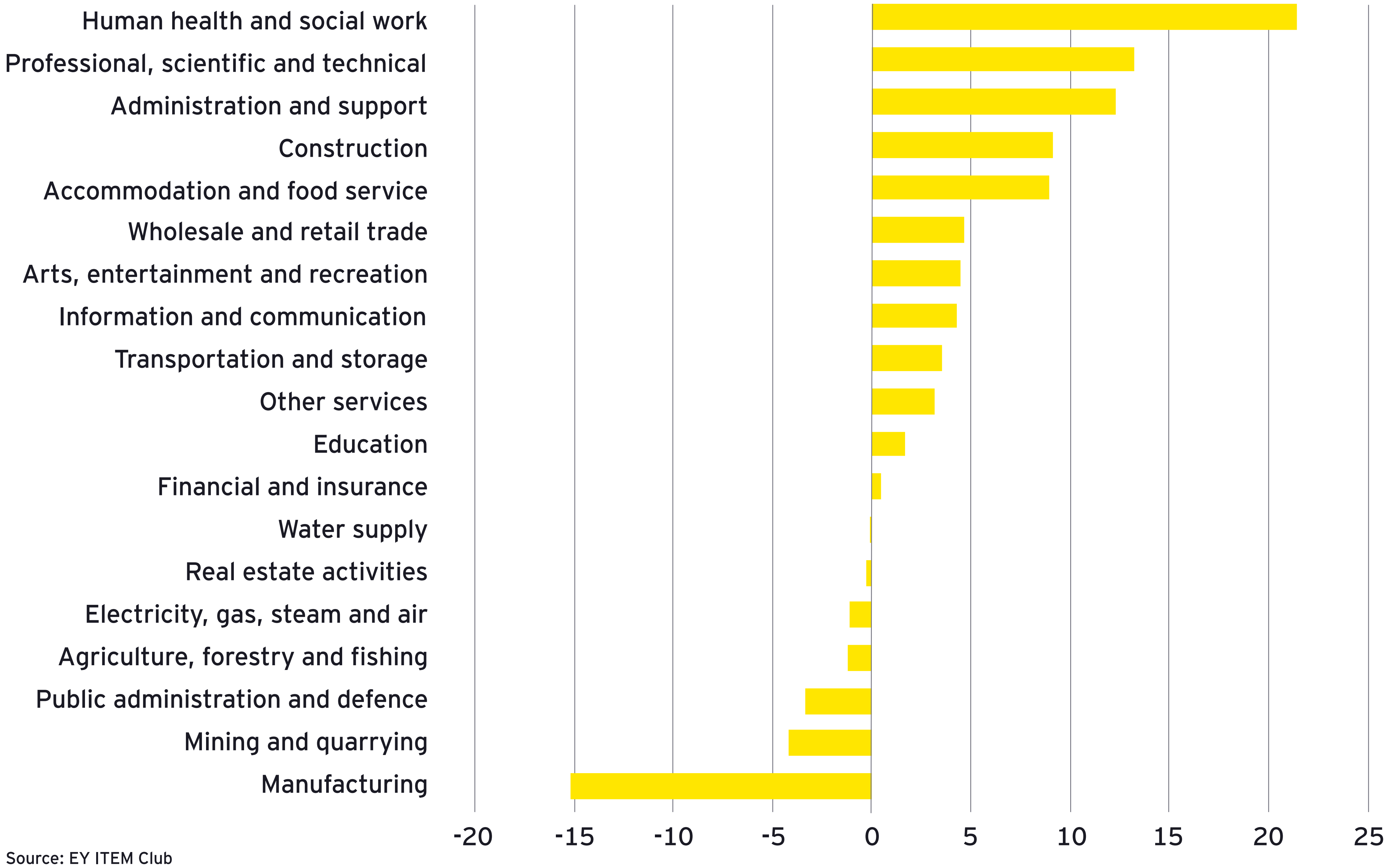
Demographic change is a key driver of employment growth in the health sector, with the ageing population expected to drive demand for health and social care services. The sector is forecast to account for over a third of new jobs created over the next five years. Private services, including professional, scientific and technical services, and administration and support, are also major contributors to longer-term employment growth in Scotland, creating over 25,000 jobs over the 2025 to 2029 period. As consumer confidence and spending build, employment in consumer services will also grow. Employment in accommodation and food services should increase by almost 9,000, with contributions of over 4,500 jobs each from wholesale and retail, and from arts, entertainment and recreation.

Sustained growth in the construction sector – driven by new homes and infrastructure projects, as well as Scotland's transition to net zero through retrofitting and renewable energy installations – is expected to support the creation of over 9,000 jobs by 2029.

There is a potential upside to the outlook for construction and engineering employment. Scottish Enterprise estimates that as many as 100,000 direct jobs could be created by Scotland achieving its net-zero ambition by 2045. However, this requires considerable investment and will also depend on skills availability, with competing demands likely across the UK, as the UK government itself seeks to drive growth by developing new infrastructure.



**Forecast employment growth by sector, 2025 to 2029 (000s)**




Source: EY ITEM Club

# US tariffs remain a risk to the forecasts

One of the big unknowns for the UK and the global economy is how trade policy will develop. The new US administration has indicated that it will impose tariffs on some US imports, with various possibilities proposed in recent weeks. However, the full scale and breadth of the policy remains unclear. One of the criteria for US tariffs is likely to be that they will be targeted at those countries with which the US operates a large trade deficit. On this basis, the UK is unlikely to be a priority, as the US currently runs a small trade surplus with the UK (according to US statistics).

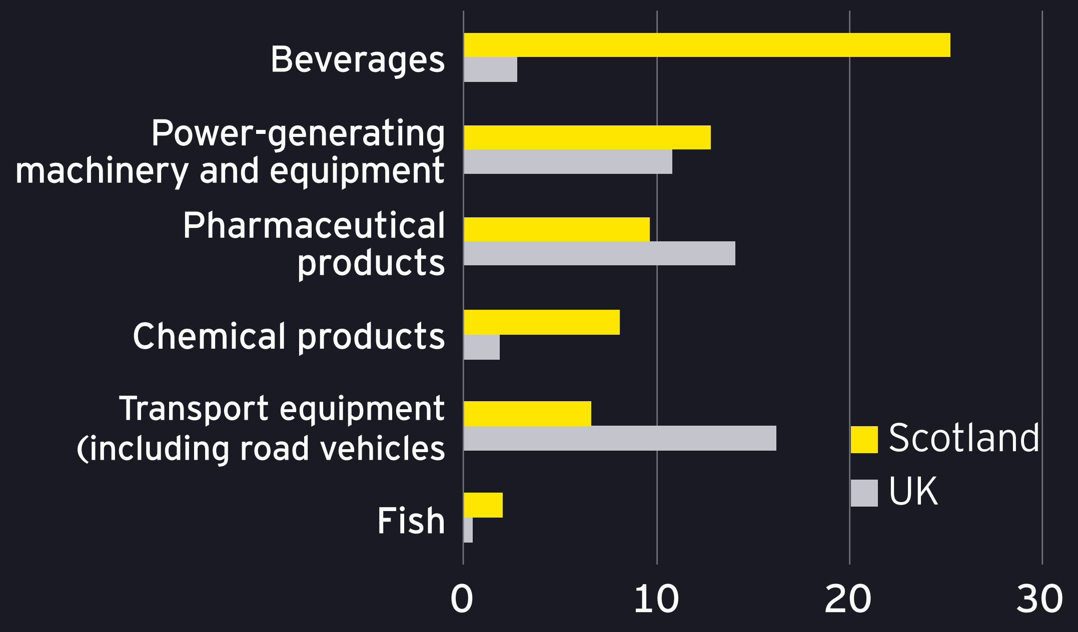
In the event of modest tariff increases, which appears to be the most likely scenario, the broader demand implications will likely be small, too. International Monetary Fund (IMF) scenario analysis estimates that if 10% of bilateral tariffs are levied between the US, China and Europe, some growth would impact the UK's key trading partners. However, the effects, particularly on Europe, are likely to be minor, with the more significant impact coming from the tighter financial conditions worldwide in recent months. Europe is the UK and Scotland's largest trading partner, which is unsurprising given its proximity. So, we estimate the indirect impact of a shift in global trade policy to be minor, too.

While the aggregate impacts may be minor, it will nonetheless mean that some sectors, and by extension UK regions and nations, are affected more than others. The pharmaceutical, transport equipment, and fishing sectors, as well as parts of the UK that are more reliant on those sectors, are some of the areas of the economy that would feel the most significant impact. Overall, Scotland is less dependent on the US as an export market than the UK, and in 2023, around 12% of Scotland's good exports were to the US compared with 15% for the UK. Whisky is Scotland's largest export to the US (25%), with power-generating machinery equipment (13%), pharmaceutical products (10%), and chemical products (8%) being the other main goods exports; transport equipment accounted for just 7% and fish just 2% of total exports. For the UK, transport equipment (including road vehicles) is the largest export to the US, accounting for 16% of the total in 2023, followed by pharmaceutical products with 14% of the total. Fish is the only more vulnerable sector where Scotland has a greater exposure, comprising 35% of UK total fish exports to the US, but the overall value is relatively small. Therefore, Scotland's exports in sectors that are more exposed to potential tariffs are relatively low.

However, with whisky accounting for such a large proportion of Scotland's goods exports and the US being by far the largest whisky export market (estimated at £978 million in 2023 and over double the next largest market of France at £474 million according to the Scotch Whisky Association), Scotland's dependence on whisky exports could therefore make it vulnerable to targeted tariffs from the US. Indeed, this happened in 2019 under the last Trump administration, when a 25% tariff was levied on all single malt whisky as part of a long-running trade dispute between the US and EU over pre-Brexit subsidies to aircraft makers. The Scotch Whisky Association claims that more than £600 million in distillery sales were lost by the time the UK and the US agreed to lift the tariffs in March 2021.

While Scotland is relatively dependent on whisky exports (accounting for 16% of total international goods exports in 2023), the responsibility for negotiating international agreements, including trade deals, is reserved for the UK government. However, the Scottish government has its own export growth strategy and aims to increase Scotland's exports from the equivalent of 20% of Scottish GDP in 2019 to 25% by 2028. The strategy involves increasing presence in key export markets, supporting exporting firms and encouraging more firms to export. However, while it is difficult to ascertain the latest position for total exports (including services), total international goods exports from Scotland have fallen by 17% in real terms between Q3 2018 and Q3 2024.

**Share of UK and Scotland goods exports to the US, 2023, %**




Source: HMRC Regional Trade Statistics (RTS)

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