

## U.S. Service Sector Expands at a Faster Pace in September

- U.S. service sector activity in September accelerated at the fastest pace since February 2023.
- The increase in services activity was driven by improvements of more than six points in both the Business Activity and New Orders indexes.
- The Employment Index slipped into contraction territory for the first time in three months, implying service sector firms reduced headcount last month.
- The Prices Paid Index rose 2.1 points to 59.4, pointing to profit margin compression in the service sector.
- Service sector activity is expected to moderate over the near term but not contract, keeping the soft-landing narrative intact.

The U.S. service sector, unlike its manufacturing counterpart, continues to expand. The ISM Services PMI improved 3.5 points to 54.9 in September. That is the third consecutive month of expansion (reading above 50) and the highest reading since February 2023. The Business Activity Index rose 6.6 points to 59.9 percent in September, signifying the third successive month of expansion after a contraction in June. The New Orders Index expanded to 59.4, 6.4 points higher than August's reading of 53.0. Conversely, the Backlog of Orders Index remained in contraction territory for the second month in a row but improved 4.6 points to 48.3.

The Employment Index slipped 2.1 points to 48.1 in September – the first contraction in three months – suggesting service sector employers reduced payrolls last month. The Suppliers Delivery Index increased 2.5 points to 52.1, pointing to slower delivery times. The Inventories Index remained in expansion territory for the second month in a row in September after two consecutive months of contraction, while the Inventory Sentiment Index fell 0.9 point but has expanded for 17 months in a row. On a more downbeat note, the Prices Paid Index rose 2.1 points to 59.4, pointing to profit margin compression in the service sector.

The acceleration in activity in the much larger service sector is a welcome development after the manufacturing sector contracted for the sixth consecutive month in September, according to the ISM Manufacturing index. While activity in the service sector is expected to moderate in the near term in concert with slower GDP growth and rising unemployment, the service sector will continue to expand as the U.S. economy experiences a soft landing and avoids recession.

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