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(Reuters) - China's services sector expanded modestly in June with the vast construction industry acting as a drag on output, in a further sign that the world's second-largest economy is losing momentum.

A lackluster services sector will not help buffer a deeper slowdown in manufacturing at a time when China's top leaders appear reluctant to loosen the policy reins to shore up growth.

A pair of Purchasing Managers Indices (PMIs) on Wednesday stayed above the watershed line of 50, which divides expansion from contraction but the readings were not strong enough to calm worries about China's slowdown. Asian shares extended losses after the surveys.

“The underlying growth momentum is likely to be softening for services sectors, along with the slowdown of manufacturing growth,” said Qu Hongbin, HSBC's China chief economist.

The headline services PMI published by the National Bureau of Statistics slipped to a 9-month low of 53.9 in June from May's 54.3, and the reading from a Markit/HSBC survey improved a touch to 51.3 from 51.2 in May.

“The slight drop in the services sector was mainly caused by a seasonal fall in the construction industry,” said Cai Jin, a vice president at the China Federation of Logistics and Purchasing (CFLP), in a statement accompanying the data.

The sub-index for construction fell to 59.3 from 62.2 in May. The CFLP conducts the official survey together with the NBS.

China's services sector accounted for 46 percent of the economy in 2012. It overtook manufacturing as the biggest employer in the country in 2011 and so far service businesses have
fared better than Chinese factories which are hurting from slackening foreign and domestic demand, as well as excess capacity.

However, economists warned sooner or later the slackening of manufacturing activity and toughening economic conditions will also catch up with the service economy.

"Employment will only worsen in the next few months, it won't improve," said Hao Zhou, an economist with ANZ in Shanghai. "Company profits are declining and they are investing less. How can employment improve?" he added.

Two separate PMI surveys on Monday showed China's manufacturing growth plumbed multi-month lows in June as foreign and domestic demand waned.

China's economic downturn, shaping up to be the worst in at least 14 years, is starting to bite. Many analysts believe the economy is backsliding into another downturn after a short-lived recovery lasting only around three months, with growth possibly even missing Beijing's 7.5 percent target this year.

An increasing show of reluctance by top Chinese leaders to take policy steps to stimulate growth has also raised the chance that China's economic downcycle may turn out worse than thought.

Indeed, an unprecedented cash crunch in China's financial markets last month, that saw interest rates briefly spike to record highs, may further drag on the economy in coming months.

JOBS UNDER PRESSURE

The official services PMI showed new orders picked up to 50.3 in June from May's 50.1 and a sub-index measuring employment rose to 51.5 from 51.3 in May.

However, in the HSBC survey, the reading for new orders fell to 50.5 in June, the lowest since November 2008. The employment sub-index in the HSBC poll showed employment improved for the second consecutive month in June, but it was not clear whether the improvement could be sustained.

"With sluggish growth of new orders, employment growth is under pressure," HSBC's Qu said.

The HSBC survey captures smaller firms more vulnerable to a slowdown while the official survey includes larger and state-owned companies who can withstand global weakness better.

Employment is a decisive factor shaping China's government policy because it is crucial for social stability.

The job market has held up so far in spite of slowing growth, explaining in part Beijing's ease with the country's fizzling economic growth momentum.

"Growth in the services sector slowed, but didn't slide," said Wei Yao, China economist of Societe Generale in Hong Kong. "It explained why the labor market has so far remained healthy."

"It ... leaves Beijing more room to tolerate economic slowdown and press ahead with structural reforms," she added.

China's President Xi Jinping said over the weekend that officials should no longer be evaluated against economic growth but with consideration to other indicators including welfare and ecological improvements and social development.
(Additional reporting by Langi Chiang and Jenny Su; Editing by Jacqueline Wong)