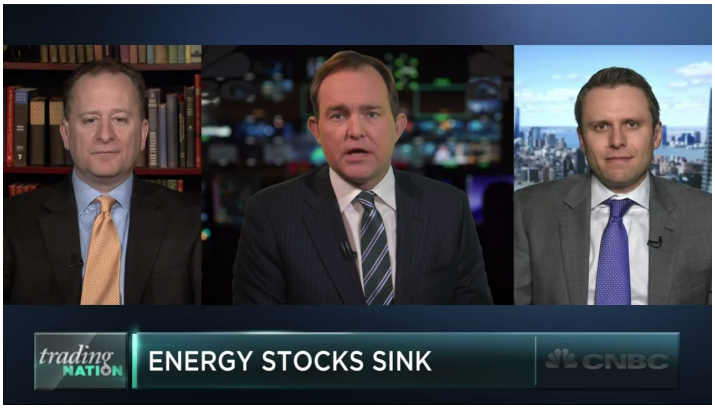
The energy sector is nearing a 'critical' level. Here's why.

Rebecca Ungarino | @ungarino
Tuesday, 31 Jan 2017 | 7:20 AM ET



Energy, the second worst-performing sector in the S&P 500 this year, could see further pain.

Chevron, one of the top-weighted holdings in a popular energy ETF (the XLE) fell nearly 2 percent on Monday after posting disappointing quarterly earnings Friday, and Exxon Mobil and Schlumberger closed down about 1 percent each. Crude oil, which has generally moved in tandem with energy names for the last year, has fallen 2 percent in 2017.

In a note Monday, Miller Tabak managing director Matt Maley said the XLE is nearing a critical multiyear trend line that if broken could mean the energy sector "is getting quite close to a compelling decline."

In addition, some strategists noted, futures traders' crude oil positions as expressed in commitment of trader data are at historic extremes, with their longest positions on record. This is quite the contrarian indicator, Maley wrote, as the "specs" are "almost always wrong at extremes."

"In other words, there are A LOT of people on the bullish side of the boat in crude oil," Maley wrote, while "commercials" in the energy space have their largest short positions ever.

The extreme positioning gives pause to Jonathan Krinsky, chief market technician at MKM Partners, who sees downside ahead for energy.

"Now when you talk about energy stocks, you have to remember it was the best-performing sector last year, but most of that was a function of a reversal of it being the worst-performing sector for much of 2014 and 2015. And the bulk of that gain came in the early part of last year. So if you weren't overweight energy stocks by April, you missed out on most

TRADING NATION

Is the dollar's run done? Why some traders say yes

The dollar finished the week just barely positive, and some strategists see the greenback heading lower.

These 'red flags' are pointing to a market drop, trader warns

One trader sees "red flags" that the market rally is about to come to a pause.

Here's why surging tech stocks might be badly overbought

Tech has been leading the best-performing sector this year, but it may be overpriced now.

Volatility hits 55-year low

By some measures, this is the quietest quarter for stocks since 1962. Boris Schlossberg of BK Asset Management and Gina Sanchez of Chantico Global discuss with Brian Sullivan.

MORE FROM TRADING NATION

This country's stocks prove to be one of the best ETF bets
February flurry: Gold, stocks and the dollar are doing something very unusual
This hot group of stocks is pennies away from a 'critical' level, strategist says
It's about to get even better for the banks, says top analyst Dick Bove
Trump's policies could lead to a big market drop, Jeremy Siegel warns
Technical analyst who correctly called for a market breakout now sees this
Dow 22K is closer than you think—here's why: Jeremy Siegel
Here are some mind-blowing stats about Apple's incredible run
Canadian stocks are heading north, and one trader sees even more gains
Here's why it could be time to short gold: Trader

LATEST SPECIAL REPORTS ›

Snapchat IPO

of the outperformance," Krinsky said Monday on CNBC's "Trading Nation."

And now, Krinsky said, the opposite is occurring; the XLE relative to the S&P 500 as well as on an absolute basis is beginning to break down below its uptrend line back to early 2015, echoing some of Maley's sentiment.

However, Eddy Elfenbein, editor of the Crossing Wall Street blog, likes energy at this juncture in light of recently agreed-upon production cuts from OPEC.

"I think it's just an unwinding of some of the recent trades. I mean, oil has had a spectacular year since the lows of about a year ago," Elfenbein said Monday on CNBC's "Trading Nation."

The XLE is up 25 percent in the last year. Elfenbein noted the energy sector's poor performance over the last seven weeks or so, but sees upside in roughly six months to a year as crude oil production cuts will take some time to play out.

"The key, this is the big game changer is that the OPEC cuts that they announced in November, these were the first major cuts in eight years, they're actually working. OPEC... they never cooperate. And it really is working this time," Elfenbein said, adding that such cuts had put a "floor" of sorts at the $50 a barrel level.

Still, the technicals in Krinsky's eyes don't appear promising.

"We don't think it's going to be anything like we saw in 2015, but [the] XLE probably has some more downside, lower to mid-60s," Krinsky said, adding that although the ETF is still well above its 200-day moving average, the extreme positions are reason enough to believe underperformance will continue in the near term.

Rebecca Ungarino
Associate Producer

RELATED SECURITIES

Symbol	Price	Change	%Change
CVX	110.33 ▼	-0.35	-0.32%
XLE	71.97 ▼	-0.40	-0.55%

ABOUT TRADING NATION

Trading Nation will offer enthusiast traders insights from a group of "Trader Coaches," a collection of expert CNBC Contributors who are well-versed in the daily challenges of trading. Each "Trader Coach" will have a different area of expertise, and will share their unique perspective on the markets, allowing new insights to emerge from this collaboration. Trading Nation is not simply about finding that next trade; it's a forum where enthusiast traders can hear and compare investing ideas in order to build confidence in their trading decisions.

ON-AIR VIDEO ›


Trading Nation: Big week for biotech
Ari Wald, Oppenheimer, and Max Wolff, Fifty-five Capital, discuss biotech stocks with Brian Sullivan.


Trading Nation: Can the tech sector keep leading the market?
Gina Sanchez of Chantico Global and Boris Schlossberg of BK Asset Management discuss the tech sector with Brian Sullivan.


Trading Nation: How to invest in home builders
Is the housing run done? Stacey Gilbert, Susquehanna, and Matt Maley, Miller Tabak, discuss.

@TRADINGNATION

Tweets by @TradingNation

Trading Nation @TradingNation

We recently discussed the $DXY with Chantico Global's @GinaVSanchez and BK Asset Management's @Fxflow. cnb.cx/2kBPwtN

Is the dollar's run done? Why some trad…
The dollar finished the week just barely pos…
cnbc.com

12h

Trading Nation @TradingNation

The market is at its quietest since 1962, is that an opportunity for you? Find out today on TradingNation.cnbc.com!

Embed View on Twitter

HOST

Brian Sullivan
"Power Lunch" Co-Anchor

TRADING NATION TUTORIALS ›

How to use the price-to-earnings ratio
Using support and resistance levels