Executive Summary

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Introduction

The study presents the first comprehensive analysis of Spanish equity returns over 120 years, focusing on their relationship with macroeconomic conditions and long-term investment performance. The authors have reconstructed more than a century of Spanish equity performance through a new historical index, the H-IBEX, which extends the IBEX-35 series back to 1900. Using archival price and dividend data from the Madrid Stock Exchange, they analyze how stock returns interacted with inflation, economic growth, and institutional change.

Spanish equities delivered an average real return of about 3% per year, markedly below the 4–6% observed in other advanced economies due mainly to severe losses during periods of war, autarky, and 1970s–80s inflation. However, following financial liberalization, macroeconomic stabilization, and European integration in the 1980s and 1990s, returns rose sharply to 7-8% in real terms and volatility decreased. The study highlights that the evolution of Spain's capital markets mirrors the country's broader economic modernization—showing that institutional strength and stability are key to long-term investor success.

"H-IBEX" Methodology

The authors constructed an original index, the "H-IBEX" ("Historical IBEX") that covers the Spanish equity market from 1900 to 1987, linking it seamlessly to the actual IBEX-35 (which exists officially since 1992 and is back-calculated to 1987). The index was based exclusively on common stocks of the largest companies incorporated in Spain, weighted by market capitalization and adjusted for capital operations, such as stock splits, new issued and subscription rights. Then, they compared it with the official Índice General de la Bolsa de Madrid (IGBM), available since 1940 and concluded that the two indices showed almost identical returns and volatility, meaning H-IBEX is a very accurate long-term proxy for the Spanish equity market and provides a realistic historical reconstruction of what the Spanish investor could have owned in each period.

The data was collected from yearbooks and daily bulletins of the Madrid Stock Exchange. They checked all the companies traded on the Exchange each January of each year. If a company was delisted, merged, or failed, it naturally disappeared from the index the next year, and a new firm replaced it. Then, they ranked them by market capitalization. The number of companies that were in the H-IBEX was as follows: in early 1900s, the index had about 10 companies. By the 1930s, it included 34, and from 1940 onwards, it was fixed at 35 companies.

To avoid false signals, they excluded stocks that had zero price changes more than 90% of the year, keeping only actively traded, liquid stocks that represented what a real investor could actually buy and sell.

Calculating total returns: To represent what an investor truly earned:

- They added dividends to the index in the month they were paid.
- They assumed investors reinvested those dividends immediately back into the index.

Avoiding biases: The index followed strict historical-finance standards to prevent distortions:

- No survival bias: failed or delisted companies (due to bankruptcy or nationalization) were included up to their exit.
- No backfilling: they didn't "fill in" missing data retroactively.

- No sector bias: though, naturally, large firms dominated, which meant some overrepresentation — banks and railways (1900–1920s), utilities (1930s–1960s), and banks again (post-1970s).

"H-IBEX" results:

- Average total nominal return: 8.3% per year (7.8% after taxes).
- Average inflation: 5.2% → real return: 3.1% per year.
- Dividends: accounted for 56% of total returns.
- Negative real returns occurred in the 1910s, 1930s-40s, and 1970s (periods of war, political turmoil, and high inflation).
- Best decades: 1920s, 1960s, 1980s-90s — when financial liberalization and stability prevailed.

Stock Prices and Real Economy Activity

The authors tested whether the Spanish stock market behaved as a forward-looking indicator of economic performance — that is, whether stock prices rose during periods of expansion and fell before recessions.

Equity prices were strongly pro-cyclical in the "roaring 1920s", the post-war "Golden Age" (1950-74) and by the growth spurred by the European integration (1985-2008). On the other hand, they recorded sluggish or even negative growth during the Great Depression, the stagflation of the 1970s-80s, and the Great Recession after the bank debt crisis of 2008-12.

They found a positive relationship between future economic activity and stock returns over the analyzed period, with equities correctly predicting business cycles with a lead of up to 10 quarters, but their predictive power was stronger for investment than for GDP. Nevertheless, they observed a lower predictive power in the period of 1941-84,wich may suggest a decline in the quality of information transmitted by stock prices in a regime of strong financial repression. In turn, stock's predictive power reached its peak after the mid-1980s, with the financial liberalization, EU integration and the modernization of market institutions and participants, when stock prices and GDP started to move in tandem, similar to the pattern observed in developed economies. The Spanish stock market only began to reflect and anticipate real economic activity after structural reforms opened, liberalized, and internationalized the financial system.

The Impact of the Civil War

Despite a 31.6% GDP contraction in just three years, the war's impact on equity returns was surprisingly moderate compared with other major twentieth-century crises. Using the reconstructed H-IBEX index, the authors showed that investors who held stocks from July 1936 to March 1940 would have experienced nominal total returns of about +36%, largely due to dividends, but real losses ranging between −2% and −18% once adjusted for wartime inflation.

The limited damage was mainly because trading was almost entirely suspended during the war: securities markets in both Republican and Nationalist zones were closed, and investors were unable to liquidate assets. This "freezing" of portfolios prevented panic sales and large realized losses. Toward the end of the war, curb markets briefly reopened, revealing stock prices already above pre-war levels as investors anticipated recovery.

Stock Market Cycles from Repression to Liberalization

Using a detailed analysis of 29 bear and 30 bull markets between 1900 and 2020, the authors found that the Spanish market spent about 60% of its time in bullish phases and 40% in bearish ones, with expansions becoming longer and contractions shorter over time.

During the authoritarian period (1940–1980), the stock market was heavily segmented and inefficient: poor disclosure, weak regulation, and limited investor participation dampened price informativeness. Trading remained low, despite a doubling of listed firms, as off-exchange deals and outdated rules restricted liquidity.

The turning point came in the late 1980s and early 1990s, when Spain's entry into the European Community and a wave of liberalizing reforms—modern regulatory institutions, technological integration of exchanges, and the creation of Bolsas y Mercados Españoles transformed the market into a modern, transparent, and globally integrated system. As a result, equity cycles became more volatile and synchronized with international markets, reflecting Spain's transition from a closed, repressed financial regime to a liberalized and internationally competitive one.

Equities and Inflation

The study shows that in periods such as the the World Wars, Civil War, and especially the 1970s–80s stagflation Spanish equities offered little protection against inflation. Nevertheless, the situation changed from the mid-1980s onward, when Spain's entry into the European Economic Community and later the Monetary Union brought monetary stability, fiscal discipline, and financial liberalization. From that moment, equities became more resilient to inflation and generated substantial real gains: investors needed only seven years of holding to secure positive real returns in most cases. The analysis of investor cohorts confirms this transformation—those who entered the market after the reforms enjoyed sustained real appreciation of equity wealth, reversing decades of underperformance

Investment Performance in International Perspective

Spain's equity market moved from isolation and repression to liberalization and global integration, transforming from one of Europe's weakest performers to one of its most dynamic by the late 20th century. The turning point came when macroeconomic and institutional reforms aligned with market openness — confirming that capital market performance mirrors institutional maturity. The creation of the CNMV, modernization of trading systems, and entry into the EU fostered transparency, liquidity, and foreign investment. Since then, equities have offered strong and stable real returns, making Spain's market comparable to other mature European systems.

Concluding Remarks

In broader perspective, the authors connect their findings to the narrative of the "Triumph of the Optimists" (Dimson, Marsh & Staunton, 2002): despite long periods of poor performance, patient investors who held equities through Spain's institutional and economic modernization ultimately prospered. The historical lesson is clear — institutional strength, macroeconomic discipline, and openness to international capital are the foundations of sustained equity growth and investor confidence.

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