FL GROUP hf.

Consolidated Financial Statements
for the year 2006
ISK

FL GROUP hf.
Suðurlandsbraut 12
108 Reykjavík
Iceland

Reg. no. 601273-0129

Contents

Endorsement and Signatures of the Board of Directors and the CEO 3

Independent Auditors' Report 5

Consolidated Income Statement 6

Consolidated Balance Sheet 7

Consolidated Statement of Changes in Equity 8

Consolidated Statement of Cash Flows 9

Notes to the Consolidated Financial Statements 11

Endorsement and Signatures of the Board of Directors and the CEO

The consolidated financial statements of FL GROUP hf. for the year 2006 have been prepared in accordance with International Financial Reporting Standard (IFRS) as adopted by EU. The financial statements comprise the consolidated financial statements of FL GROUP hf. ("the Company") and its subsidiaries.

FL GROUP hf. is an investment company, focusing on strategic and private equity investments as well as proprietary trading. The Company focuses on investments in companies in Northern Europe on a broad basis. The company operates three offices, in Reykjavík, Copenhagen and London. The offices in Copenhagen and London were both opened during the year 2006.

In October 2006 the Company sold its subsidiary Icelandair Group hf., which is not a part of FL GROUP hf.'s consolidated financial statements from that time. Icelandair Group hf. had become the parent of almost all the Icelandic subsidiaries of FL GROUP hf. operating in the aviation and tourism industry since beginning of the year 2006. The only Icelandic subsidiaries excluded from the transfer were Ferðaskrifstofa Íslands hf. and Bílaleiga Flugleiða hf., both disposed of in the beginning of the year, and Kynnisferðir ehf. which was still a subsidiary at year end 2006.

The Company took over the operations of Sterling Airlines A/S, Flyselskabet af 15. Juli 2005 A/S and Sterling Icelandic ApS (together referred to as "Sterling"), in the beginning of January 2006 and it became a part of FL GROUP hf.'s consolidated financial statements from that time. At the end of December 2006 the Company sold Sterling and related companies to Northern Travel Holding ehf. and became a 34.8% shareholder in that Company at the same time.

According to the consolidated income statement, profit for the year amounted to ISK 44,559 million. According to the consolidated balance sheet, equity at the end of the year amounted to ISK 142,676 million, including share capital in the amount of ISK 7,763 million.

The Company's issued share capital amounted to ISK 7,945 million at the end of the year, from which the Company held own shares in the amount of ISK 182 million. The share capital was increased in January 2006 by ISK 296 million which was sold for ISK 4,022 million in relation to the purchase of Sterling. In July 2006 FL GROUP hf. acquired 24.2% share in Straumur-Burdarás Investment Bank hf. As part of the consideration paid shareholders' meeting approved to increase its share capital by ISK 1,804 million which was sold for ISK 28,322 million. Shareholders at the end of the year 2006 were 4,622, but were 5,024 at the beginning of the year, a decrease of 402 during the year. When forward agreements are taken into account, three shareholders held more than 10% of outstanding shares each at year end 2006. They are Oddaflug B.V. with 19.8% share, Baugur Group hf. with 18.2% share and Gnúpur fjárfestingafélag with 17.2% share. In addition, the share of Icon ehf. and Materia Invest ehf., which are owned by the same shareholders, was 10.7%.

The Board of Directors proposes a dividend payment amounting to ISK 15,000 million which is approximately 193% of the nominal value of share capital at year end 2006. The dividend payment therefore is 33.7 % of profit for the year. Reference is made to the notes to the consolidated financial statements regarding information on other changes in equity.

Endorsement and Signatures of the Board of Directors and the CEO, contd.:

The Board of Directors and the CEO of FL GROUP hf. hereby confirm the Company's consolidated financial statements for the year 2006 by means of their signatures.

Reykjavík, 1 February 2007.

The Board of Directors:

Skarphéðinn Berg Steinarsson

Þorsteinn M. Jónsson

Magnús Ármann

Smári Sigurðsson

Paul Davidson

CEO:

Hannes Smárason

Independent Auditors' Report

To the Board of Directors and Shareholders of FL GROUP hf.

Report on the Consolidated Financial Statements

We have audited the accompanying consolidated financial statements of FL GROUP hf. and its subsidiaries, ("the Group"), which comprise the consolidated balance sheet as at December 31, 2006, and the consolidated income statement, consolidated statement of changes in equity and consolidated cash flow statement for the year then ended, and a summary of significant accounting policies and other explanatory notes.

Management's Responsibility for the Consolidated Financial Statements

Management is responsible for the preparation and fair presentation of these consolidated financial statements in accordance with International Financial Reporting Standards as adopted by the EU. This responsibility includes: designing, implementing and maintaining internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatements, whether due to fraud or error; selecting and applying appropriate accounting policies; and making accounting estimates that are reasonable in the circumstances.

Auditor's Responsibility

Our responsibility is to express an opinion on these consolidated financial statements based on our audit. We conducted our audit in accordance with International Standards on Auditing. Those standards require that we comply with relevant ethical requirements and plan and perform the audit to obtain reasonable assurance whether the financial statements are free of material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on our judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, we consider internal control relevant to the entity's preparation and fair presentation of the consolidated financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

Opinion

In our opinion, the consolidated financial statements give a true and fair view of the financial position of the Group as at 31 December 2006, and of its financial performance and its consolidated cash flows for the year then ended in accordance with International Financial Reporting Standards as adopted the EU.

Reykjavík, 1 February 2007.

KPMG hf.

Jón S. Helgason
Sæmundur Valdimarsson

Consolidated Income Statement for the year 2006

	Notes	2006	2005
Investment income:			
Net income from securities and derivatives	10	23,956	21,958
Interest income		854	1,270
Interest expenses		(4,948)	(2,258)
Net foreign exchange loss		(2,371)	(621)
		17,491	20,349
Operating expenses	11	(2,771)	(1,652)
Profit before income tax		**14,720**	**18,697**
Tax income (expense)	14,15	2,631	(3,292)
Profit from continuing operations		**17,351**	**15,405**
Profit from discontinued operations (net of income tax)	7	27,208	1,846
Profit for the year		**44,559**	**17,251**
Attributable to:			
Equity holders of the parent		44,560	17,249
Minority interest		(1)	2
Profit for the year		**44,559**	**17,251**
Earnings per share			
Basic earnings per share (ISK)	17	6.65	5.90
Diluted earnings per share (ISK)	17	6.60	5.84

The notes on pages 11 to 39 are an integral part of these consolidated financial statements.

Amounts are in ISK million

Consolidated Balance Sheet as at 31 December 2006

	Notes	2006	2005
Assets:			
Cash and cash equivalents	18	47,022	10,350
Securities	19	181,161	69,138
Derivatives	21	4,309	6,341
Restricted cash	22	9,572	0
Assets classified as held for sale	8	904	0
Loans, trade and other receivables	23,24	19,478	7,222
Inventories		0	876
Prepaid aircraft acquisitions		0	14,490
Operating assets	25	425	20,731
Intangible assets	26	0	3,470
Total assets		262,871	132,618
Equity:			
Share capital	27	7,763	5,802
Share premium		70,530	43,169
Reserves		948	434
Retained earnings		63,425	25,027
Total equity attributable to equity holders of the parent		142,666	74,432
Minority interest		10	11
Total equity		142,676	74,443
Liabilities:			
Derivatives	21	7,021	277
Trade and other payables	28	5,908	10,895
Deferred income		0	2,641
Liabilities classified as held for sale	8	634	0
Current income tax liability		782	0
Borrowings	29,30	104,955	39,668
Deferred income tax liability	31	895	4,694
Total liabilities		120,195	58,175
Total equity and liabilities		262,871	132,618

The notes on pages 11 to 39 are an integral part of these consolidated financial statements.

Amounts are in ISK million

Consolidated Statement of Changes in Equity for the year 2006

	Share capital	Share premium	Reserves: Share option reserve	Reserves: Hedging reserve	Reserves: Translation reserve	Retained earnings	**Equity holders of the Parent**	Minority interest	**Total equity**
2005									
Equity 1.1.2005	2,525	3,609	87	(100)	(623)	9,242	**14,740**	21	**14,761**
Translation difference					802		**802**		**802**
Effective portion of changes in fair value of cash flow hedges				287			**287**		**287**
Net income recognised directly in equity				287	802		**1,089**		**1,089**
Profit for the year						17,249	**17,249**	2	**17,251**
Total profit for the year				287	802	17,249	**18,338**	2	**18,340**
Dividends (ISK 0.60 per share)						(1,466)	**(1,466)**		**(1,466)**
Issued share capital	3,308	40,839					**44,147**		**44,147**
Own shares, change	(31)	(1,440)					**(1,471)**		**(1,471)**
Stock options		161	(19)				**142**		**142**
Acquisition of minority interest								(12)	**(12)**
Equity 31.12.2005	5,802	43,169	68	187	179	25,027	**74,432**	**11**	**74,443**
2006									
Equity 1.1.2006	5,802	43,169	68	187	179	25,027	**74,432**	11	**74,443**
Translation difference					3,519		**3,519**		**3,519**
Effective portion of changes in fair value of cash flow hedges				54			**54**		**54**
Hedging and translation reserves transferred to profit and loss				(241)	(2,910)		**(3,151)**		**(3,151)**
Net income recognised directly in equity				(187)	609		**422**		**422**
Profit for the year						44,560	**44,560**	(1)	**44,559**
Total profit for the year				(187)	609	44,560	**44,982**	(1)	**44,981**
Dividends (ISK 1.04 per share)						(6,341)	**(6,341)**		**(6,341)**
Issued share capital	2,100	30,244					**32,344**		**32,344**
Own shares, change	(139)	(2,980)					**(3,119)**		**(3,119)**
Translation reserve 1.1.2006 transferred					(179)	179	**0**		**0**
Stock options		97	271				**368**		**368**
Equity 31.12.2006	7,763	70,530	339	0	609	63,425	**142,666**	10	**142,676**

The notes on pages 11 to 39 are an integral part of these consolidated financial statements.

Amounts are in ISK million

Consolidated Statement of Cash Flows for the year 2006

	Notes	2006	2005
Cash flows from operating activities:			
Profit for the year		44,559	17,251
Adjustments for:			
Depreciation		23	2,408
Other operating items		784	(16,093)
Discontinued operations	7	1,982	0
Working capital from operations		47,348	3,566
Net change in operating assets and liabilities		(1,099)	1,855
Net cash provided by operating activities		46,249	5,421
Cash flows from investing activities:			
Securities, change		(92,518)	(24,607)
Acquisition of subsidiary, net of cash acquired	9	(9,399)	(2,626)
Disposals of subsidiaries, net of cash sold	7	29,304	0
Derivatives, change		8,776	0
Restricted cash, change		(9,572)	0
Trade receivables and bonds		8,274	0
Acquisition of operating assets		(448)	(18,157)
Proceeds from the sale of operating assets		0	5,269
Acquisition of intangible assets		0	(113)
Discontinued operations	7	2,822	0
Net cash used in investing activities		(62,761)	(40,234)
Cash flows from financing activities:			
Proceeds from the issue of share capital		0	24,399
Own shares, change		(3,119)	(1,471)
Dividend paid		(6,341)	(1,466)
Proceeds from borrowings		133,271	24,190
Repayment of borrowings		(72,566)	(3,916)
Discontinued operations	7	(584)	0
Net cash provided by financing activities		50,661	41,736
Net increase in cash and cash equivalents		34,149	6,923
Cash and cash equivalents at 1 January		10,350	2,819
Effect of exchange rate fluctuations on cash held		2,523	608
Cash and cash equivalents at 31 December		47,022	10,350
Investing and financing transactions without cash flow effect:			
Acquisition of securities		(28,322)	(19,513)
Acquisition of subsidiary		(4,022)	0
Issued share capital		32,344	19,513

Amounts are in ISK million

Consolidated Statement of Cash Flows for the year 2006, contd.:

Other information:

Interest income received	818	1,105
Interest expense paid	2,663	1,956
Income taxes paid	0	0
Dividends received	806	0

The notes on pages 11 to 39 are an integral part of these consolidated financial statements.

Notes to the Consolidated Financial Statements

1. **Reporting Entity**

FL GROUP hf.'s registered office is at Suðurlandsbraut 12 in Reykjavík, Iceland. The consolidated financial statements of FL GROUP hf. ("the Company") as at and for the year ended 31 December 2006 comprise the Company and its subsidiaries, together referred to as the “Group”.

FL GROUP hf. is an investment company, focusing on strategic and private equity investments as well as proprietary trading. The Company focuses on investments in companies in Northern Europe on a broad basis. The company operates three offices, in Reykjavík, Copenhagen, and London. The offices in Copenhagen and London were both opened during the year 2006. The Company is listed on the Iceland Stock Exchange.

2. **Basis of preparation**

Assets and liabilities in the Balance Sheet are presented in liquidity order which is considered more appropriate for the Group than the current/non-current presentation. For each asset and liability item that combines amounts expected to be recoverd or settled after more than 12 months, a payment schedule is disclosed.

a. ***Statement of compliance***

The consolidated financial statements have been prepared in accordance with International Financial Reporting Standards (IFRSs) as adopted by EU.

The financial statements were approved by the Board of Directors of FL GROUP hf. on 1 February 2007.

b. ***Basis of measurement***

The consolidated financial statements are prepared on the historical cost basis except for the following:

* derivative financial instruments are measured at fair value;
* financial instruments at fair value through profit or loss are measured at fair value;
* investments in associates are measured at fair value.

c. ***Functional and presentation currency***

The consolidated financial statements are prepared in Icelandic Krona (ISK), which is the Company's functional currency for the year 2006. All financial information has been rounded to the nearest million.

The Company’s functional currency for the year 2005 was the US dollar. The change in functional currency from US dollar to Icelandic Krona was made as of 1 January 2006 because of changes in the focus of the Company’s operations and primary economic environment in which the Company operates. The comparative figures for the year 2005 have been translated to ISK.

d. ***Use of estimates and judgements***

The preparation of financial statements requires management to make judgements, estimates and assumptions that affect the application of accounting policies and the reported amounts of assets, liabilities, income and expenses. Actual results may differ from these estimates.

Estimates and underlying assumptions are reviewed on an ongoing basis. Revisions to accounting estimates are recognised in the period in which the estimate is revised and in any future periods affected.

In particular, information about significant areas of estimation uncertainty and critical judgements in applying accounting policies that have the most significant effect on the amount recognised in the financial statements is described in note 4j.

3. Accounting policies related to financial instruments

a. *Financial instruments*

(i) *Non-derivative financial instruments*

Non-derivative financial instruments in the Group´s balance sheet comprise securities, loans, trade and other receivables, cash and cash equivalents, restricted cash, borrowings, trade and other payables and ordinary shares.

Non-derivative financial instruments are recognised initially at fair value plus, for instruments not at fair value through profit or loss, any directly attributable transaction costs. Subsequent to initial recognition non-derivative financial instruments are measured as described below.

A financial instrument is recognised if the Group becomes a party to the contractual provisions of the instrument. Financial assets are derecognised if the Group's contractual rights to the cash flows from the financial assets expire or if the Group transfers the financial asset to another party without retaining control or substantially all risks and rewards of the asset. Regular way purchases and sales of financial assets are accounted for at trade date, i.e. the date that the Group commits itself to purchase or sell the asset. Financial liabilities are derecognised if the Group's obligations specified in the contract expire or are discharged or cancelled.

Cash and cash equivalents comprise cash balances, demand deposits and mutual-fund certificates that are readily convertible to known amounts of cash and are subject to an insignificant risk of changes in value.

Restricted cash comprise of cash collaterals held by counterparties as guarantee for derivative transactions.

Accounting for finance income and expense is discussed in note 3c.

Investments at fair value through profit and loss

Securities in the balance sheet are financial assets classified as at fair value through profit or loss and designated as such upon initial recognition. Financial assets are designated at fair value through profit or loss if the Group manages such investments and makes purchase and sale decisions based on their fair value. Upon initial recognition, attributable transaction costs are recognised in profit or loss when incurred. Financial instruments at fair value through profit or loss are measured at fair value, and changes therein are recognised in profit or loss.

Other

Other non-derivative financial instruments are measured at amortised cost using the effective interest method, less any impairment losses.

(ii) *Derivative financial instruments*

The Group holds derivative financial instruments for investment purposes but also to hedge its interest rate risk exposures. Embedded derivatives are separated from the host contract and accounted for separately if the economic characteristics and risks of the host contract and the embedded derivative are not closely related, a separate instrument with the same terms as the embedded derivative would meet the definition of a derivative, and the combined instrument is not measured at fair value through profit or loss.

Derivatives are recognised initially at fair value; attributable transaction costs are recognised in profit or loss when incurred. Subsequent to initial recognition, derivatives are measured at fair value, and changes therein are accounted for through profit or loss. Derivatives with positive fair value at the reporting date are recognised as assets in the balance sheet while derivatives with negative fair value are recognised as liabilities.

(ii) contd.:

Hedge accounting is not applied at year end 2006.

(iii) *Share capital*

Ordinary shares
Incremental costs directly attributable to issue of shares and share options are recognised as a deduction from equity.

Repurchase of share capital
When share capital recognised as equity is repurchased, the amount of the consideration paid, including directly attributable costs, is recognised as a deduction from equity. Repurchased shares are classified as treasury shares and are presented as a deduction from total equity.

Dividends
Dividends are recognised as a decrease in equity in the period in which they are declared.

b. *Fair value measurement principles for financial instruments*

(i) *Securities*

Securities in the balance sheet consist of investments in equity and debt securities. The fair value of securities is based on their quoted market bid prices at the reporting date without any deduction for estimated future selling costs.

If a quoted market price is not available on a stock exchange or from a broker / dealer for non-exchange-traded financial instruments, the fair value of the investment is estimated using valuation techniques, including use of recent arm's length market transactions, reference to the current fair value of another instrument that is substantially the same, discounted cash flow techniques, option pricing models or any other valuation technique that provides a reliable estimate of prices obtained in actual market transactions.

Where discounted cash flow techniques are used, estimated future cash flows are based on management's best estimates and the discount rate used is a market rate at the reporting date applicable for an instrument with similar terms and conditions. Where other pricing models are used, inputs are based on market data at the reporting date. Fair values for unquoted equity investments are estimated, if possible, using applicable price / earnings ratios for similar listed companies adjusted to reflect the specific circumstances of the issuer.

(ii) *Derivatives*

The fair value of forward exchange contracts are based on their listed market price, if available. If a listed market price is not available, then fair value is estimated by discounting the difference between the contractual forward price and the current forward price for the residual maturity of the contract using a risk-free interest rate based on government bonds.

The fair value of interest rate swaps is based on broker quotes. Those quotes are tested for reasonableness by discounting estimated future cash flows based on the terms and maturity of each contract and using market interest rates for a similar instrument at the measurement date.

(iii) *Loans, trade and other receivables*

The fair value of loans, trade and other receivables, which is determined for disclosure purposes, is estimated as the present value of future cash flows, discounted at the market rate of interest at the reporting date.

(iv) *Non-derivative financial liabilities*

The fair value of non-derivative financial liabilities which is determined for disclosure purpose is based on the present value of future principal and interest cash flows, discounted at the market rate of interest at the reporting date.

c. *Investment income*

(i) *Net income from securities and derivatives*

Net income from investments in securities and derivatives comprise gain on the sale of shares, changes in the fair value of the investments and derivatives, other than foreign exchange hedges, and dividend income. Dividend income is recognised in the income statement on the date the entity's right to receive payments is established.

(ii) *Interest income and expense*

Interest income and expense is recognised in the income statement, using the effective interest method.

(iii) *Net foreign exchange (loss) gain*

Net foreign exchange (loss) gain comprises foreign exchange changes arising from assets and liabilities denominated in foreign currencies and gains and losses arising from derivatives hedging the foreign currency risk.

4. Other accounting policies

a. *Basis of consolidation*

(i) *Subsidiaries*

Subsidiaries are entities controlled by the Company. Control exists when the Company has the power, directly or indirectly, to govern the financial and operating policies of an entity so as to obtain benefits from its activities. In assessing control, potential voting rights that presently are exercisable or convertible are taken into account. The financial statements of subsidiaries are included in the consolidated financial statements from the date that control commences until the date that control ceases.

(ii) *Associates*

Associates are those entities in which the Group has significant influence, but not control, over the financial and operating policies. Investments in associates are designated at fair value through profit or loss on initial recognition and are included in the item securities in the balance sheet. The Group defines its operations partly as venture capital organisation and that part of the business is clearly and objectively distinct from other operations.

(iii) *Transactions eliminated on consolidation*

Intra-group balances and any unrealised income and expenses arising from intra-group transactions, are eliminated in preparing the consolidated financial statements.

b. *Foreign currency*

(i) *Foreign currency transactions*

Transactions in foreign currencies are translated to the respective functional currency of Group entities at exchange rates ruling at the dates of the transactions. Monetary assets and liabilities denominated in foreign currencies at the reporting date are translated to the functional currency at the exchange rate ruling at that date. Foreign exchange differences arising on translation are recognised in the income statement. Acquisition of operating assets in foreign currencies is translated at the foreign exchange rate ruling at the date of the transaction. Operating expenses and sales in foreign currencies are translated at the foreign exchange rate ruling at the date of the transaction.

(ii) *Foreign operations*

The assets and liabilities of foreign operations, including goodwill and fair value adjustments arising on acquisition, are translated to the functional currency at exchange rates at the reporting date. The income and expenses of foreign operations are translated to the functional currency at the average exchange rate.

Foreign currency differences are recognised directly in equity in the foreign currency translation reserve. When a foreign operation is disposed of, in part or in full, the relevant amount in the foreign currency translation differences is transferred to profit or loss.

c. ***Operating assets***

(i) *Aircrafts and flight equipment*

Aircrafts and flight equipment are stated at cost less accumulated depreciation and impairment losses. When aircrafts are acquired, the purchase price is divided between the aircraft itself and engines. Aircrafts are depreciated over the estimated useful life of the relevant aircraft until a residual value is met. Engines are depreciated according to flown hours. When an engine is overhauled the cost of the overhaul is capitalised and the remainder of the cost of the previous overhaul that has not already been depreciated, if any, is expensed in full.

(ii) *Buildings and other operating assets*

Buildings and other operating assets are stated at cost less accumulated depreciation and impairment losses.

(iii) *Subsequent costs*

The cost of replacing part of an item of operating asset is recognised in the carrying amount of the item if it is probable that the future economic benefits embodied with the item will flow to the Group and the cost of the item can be measured reliably. All other costs are recognised in the income statement as an expense as incurred.

(iv) *Depreciation*

Depreciation is charged to the income statement on a straight-line basis over the estimated useful lives of each item of operating assets. The estimated useful lives are as follows:

Aircrafts and flight equipment	10-25 years
Engines	Flying hours
Buildings	15-50 years
Other operating assets	3-8 years

The depreciation method, useful lives and residual values are reassesed at the reporting date.

d. ***Impairment***

(i) *Financial assets*

Financial assets that are stated at cost or amortised cost are reviewed at each reporting date to determine whether there is objective evidence of impairment. If any such indication exists, an impairment loss is recognised in the income statement as the difference between the asset’s carrying amount and the present value of estimated future cash flows discounted at the financial asset’s original effective interest rate.

If in a subsequent period the amount of an impairment loss recognised on a financial asset carried at amortised cost decreases and the decrease can be linked objectively to an event occurring after the write-down, the write-down is reversed through the income statement.

(ii) *Non-financial assets*

The carrying amounts of the Group's non-financial assets are reviewed at each reporting date to determine whether there is any indication of impairment. If any such indication exists then the asset's recoverable amount is estimated.

An impairment loss is recognised if the carrying amount of an asset or its cash-generating unit exceeds its recoverable amount. A cash-generating unit is the smallest identifiable asset group that generates cash flows that largely are independent from other assets and groups. Impairment losses are recognised in profit or loss. Impairment losses recognised in respect of cash-generating units are allocated first to reduce the carrying amount of any goodwill allocated to the units and then to reduce the carrying amount of the other assets in the unit (group of units) on a pro rata basis.

The recoverable amount of an asset or cash-generating unit is the greater of its value in use and its fair value less costs to sell. In assessing value in use, the estimated future cash flows are discounted to their present value using a pre-tax discount rate that reflects current market assessments of the time value of money and the risks specific to the asset.

An impairment loss in respect of goodwill is not reversed. In respect of other assets, impairment losses recognised in prior periods are assessed at each reporting date for any indications that the loss has decreased or no longer exists. An impairment loss is reversed if there has been a change in the estimates used to determine the recoverable amount. An impairment loss is reversed only to the extent that the asset's carrying amount does not exceed the carrying amount that would have been determined, net of depreciation or amortisation, if no impairment loss had been recognised.

(iii) *Assets classified as held for sale*

Non-current assets or disposal groups, comprising assets and liabilities, that are expected to be recovered primarily through sale rather than through continuing use are classified as held for sale. Immediately before classification as held for sale, the assets (or components of a disposal group) are remeasured in accordance with the Group's accounting policies. Thereafter, generally the disposal group is measured at the lower of their carrying amount and fair value less cost to sell. Any impairment loss on a disposal group first is allocated to goodwill, and then to remaining assets and liabilities on pro rata basis, except that no loss is allocated to inventories and financial assets which continue to be measured in accordance with the Group's accounting policies. Impairment losses on initial classification as held for sale and subsequent gains or losses on remeasurement are recognised in profit or loss. Gains are not recognised in excess of any cumulative impairment loss.

Assets and disposal groups, comprising assets and liabilities, classified as held for sale are presented in special line items in the balance sheet.

e. *Share-based payment transactions*

The grant date fair value of options granted to employees is recognised as an employee expense, with a corresponding increase in equity, over the period in which the employees become unconditionally entitled to the options. The amount recognised as an expense is adjusted to reflect the actual number of share options that vest.

The fair value of employee stock options is measured using a Black-Scholes model. Measurement inputs include share price on measurement date, exercise price of the instrument, expected volatility based on weighted average historic volatility adjusted for changes expected due to publicly available information, weighted average expected life of the instruments based on historical experience and general option holder behaviour, expected dividends, and the risk-free interest rate based on government bonds. Service and non-market performance conditions attached to the transactions are not taken into account in determining fair value.

f. ***Income tax expense***

Income tax on the profit or loss for the year comprises current tax and deferred tax.

Current tax is the expected tax payable on the taxable income for the year, using tax rates enacted or substantially enacted at the reporting date, and any adjustment to tax payable in respect of previous years.

Deferred tax is provided using the balance sheet method, providing for temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for taxation purposes. The following temporary differences are not provided for: goodwill not deductible for tax purposes, the initial recognition of assets or liabilities that affect neither accounting nor taxable profit, and differences relating to investments in subsidiaries to the extent that they will probably not reverse in the foreseeable future. The amount of deferred tax provided is based on the expected manner of realisation or settlement of the carrying amount of assets and liabilities, using tax rates enacted or substantively enacted at the reporting date.

g. ***Earnings per share***

The Group presents basic and diluted earnings per share (EPS) data for its ordinary shares. Basic EPS is calculated by dividing the profit attributable to ordinary shareholders of the Company by the weighted average number of ordinary shares outstanding during the year. Diluted EPS is determined by adjusting the profit or loss attributable to ordinary shareholders and the weighted average number of ordinary shares outstanding for the effects of all dilutive potential ordinary shares. Earnings per share are disclosed separately for continuing and discontinued operations.

h. ***Segment reporting***

A segment is a distinguishable component of the Group that is engaged in providing products or services and which is subject to risks and rewards that are different from those of other segments. The Group´s primary format for segment reporting is based on matrix presentation, which includes business and geographical segments.

i. ***New standards and interpretations not yet adopted***

A number of new standards, amendments to standards and interpretations are not yet effective for the year ended 31 December 2006, and have not been applied in preparing these consolidated financial statements:

IFRS 7 Financial Instruments: Disclosures and the Amendment to IAS 1 Presentation of Financial Statements: Capital Disclosures require extensive disclosures about the significance of financial instruments for an entity's financial position and performance, and qualitative and quantitative disclosures on the nature and extent of risks. IFRS 7 and amended IAS 1, which become mandatory for the Group's 2007 financial statements, will require extensive additional disclosures with respect to the Group's financial instruments and share capital.

IFRS 8 Operating Segments sets out requirements for disclosure of information about an entity's operating segments and also about the entity's products and services, the geographical areas in which it operates, and its major customers. If adopted by the EU, IFRS 8, which becomes mandatory for the Group's 2009 financial statements, is not expected to have any impact on the consolidated financial statements.

i. contd.:

IFRIC 7 Applying the Restatement Approach under IAS 29 Financial Reporting in Hyperinflationary Economies addresses the application of IAS 29 when an economy first becomes hyperinflationary and in particular the accounting for deferred tax. IFRIC 7, which becomes mandatory for the Group's 2007 financial statements, is not expected to have any impact on the consolidated financial statements.

IFRIC 8 Scope of IFRS 2 Share-based Payment addresses the accounting for share-based payment transactions in which some or all of goods or services received cannot be specifically identified. IFRIC 8 will become mandatory for the Group's 2007 financial statements, with retrospective application required. The Group has not yet determined the potential effect of the interpretation.

IFRIC 9 Reassessment of Embedded Derivatives requires that a reassessment of whether embedded derivative should be separated from the underlying host contract should be made only when there are changes to the contract. IFRIC 9, which becomes mandatory for the Group's 2007 financial statements, is not expected to have any impact on the consolidated financial statements.

IFRIC 10 Interim Financial Reporting and Impairment prohibits the reversal of an impairment loss recognised in a previous interim period in respect of goodwill, an investment in an equity instrument or a financial asset carried at cost. If adopted by the EU, IFRIC 10, will become mandatory for the Group's 2007 financial statements.

IFRIC 11 IFRS 2 Group and Treasury Share Transactions deals with how certain types of agreements on securities related payments shall be recognized in the financial statements of a company and its subsidiaries. If adopted by the EU, IFRIC 11 applies for accounting periods starting as of March 1, 2007.

IFRIC 12 Service Concession Arrangements. If adopted by the EU, IFRIC 12 will become mandatory for the Group's 2007 financial statements. IFRIC 12 is not expected to have any impact on the consolidated financial statements of the Group.

j. ***Accounting estimates and judgements***

Key sources of estimation uncertainty

Determination of fair values of financial instruments

As indicated in note 3b the Group's securities, derivatives and investments in associates are measured at fair value on the balance sheet. For the majority of these financial instruments, quoted market prices are readily available. However, certain financial instruments, for example, over-the-counter derivatives or unquoted securities are fair valued using valuation techniques, including reference to the current fair values of other instruments that are substantially the same, subject to the appropriate adjustments.

Fair value estimates are made at a specific point in time, based on market conditions and information about the financial instrument. These estimates are subjective in nature and involve uncertainties and matters of significant judgement (e.g. interest rates, volatility, estimated cash flows etc.) and therefore, cannot be determined with precision.

Determination of impairment of financial assets

Assets accounted for at amortised cost are evaluated for impairment on the basis described in accounting policy 4d(i). The assessment for impairment is based upon management's best estimate of the present value of the cash flows that are expected to be received. In estimating these cash flows, management makes judgements about a counterparty's financial situation and the net realisable value of any underlying collateral.

Determination of impairment of non-financial assets, contd.:

Non-financial assets, such as goodwill and intangible assets, are regularily waluated for impairment. The assessment for impairment is based upon management's estimates of future cash flows and discount rate.

Determination of fair value of share-based payment transactions

The fair value of options at grant date is determined as disclosed in accounting policy 4e. For share options granted to employees, in many cases market prices are not available, because the options granted are subject to terms and conditions that do not apply to traded options. If traded options with similar terms and conditions do not exist, the fair value of the options granted are estimated by applying an option pricing model. In estimating the fair value of options at grant date, the management considers factors that knowledgeable, willing market participants would consider in selecting the option pricing model to be used for this purpose.

Critical accounting judgements in applying the Group's accounting policies

Classification of securities

The Group's accounting policies provide scope for securities to be designated at fair value through profit or loss. By making this designation, the management has determined that it has met the necessary criteria as set out in accounting policy 3a(i).

Classification of assets as held for sale

Certain assets and related liabilities are classified as held for sale as described in note 4d(iii). By making this classification, the management has determined that their carrying amount will be recovered principally through a sale transaction rather than through continuing use. Furthermore, the management expects the sale to be completed within one year from the date of classification and that it is unlikely that significant changes will be made to the planned sale. However, future events or circumstances may extend the period to complete the sale beyond one year or they may lead to the assets no longer meeting the requirements for classification as held for sale.

Deferred tax assets

Deferred tax assets are recognised for most deductible temporary differences and for tax losses carried forward to the extent that it is probable that taxable profit will be available against which they can be utilized. Significant management judgement is required to determine the amount of deferred tax assets that can be recognized, based on the likely timing and level of future taxable profits together with future tax planning strategies.

5. Accounting policies related to discontinued operations

a. *Discontinued operations*

A discontinued operation is a component of the Group's business that represents a separate major line of business that has been disposed of or is classified held for sale. Classification as a discontinued operation occurs upon disposal or when the operation meets the criteria to be classified as held for sale, if earlier. When an operation is classified as a discontinued operation, the comparative income statement is restated as if the operation had been discontinued from the start of the comparative period.

b. *Inventories*

Goods for resale and supplies are stated at the lower of cost and net realisable value. Net realisable value is the estimated selling price in the ordinary course of business, less the estimated costs of completion and selling expenses. Aircraft equipment is capitalised at the foreign exchange rate ruling at the date of acquisition.

c. ***Intangible assets***

(i) *Goodwill and intangible assets with indefinite useful lives*

All business combinations are accounted for by applying the purchase method. Goodwill represents amounts arising on acquisition of subsidiaries. In respect of business acquisitions goodwill represents the difference between the cost of the acquisition and the fair value of the net identifiable assets acquired.

Goodwill and trademarks with indefinite useful lives are stated at cost less accumulated impairment losses.

(ii) *Other intangible assets*

Other intangible assets are stated at cost less accumulated amortisation and impairment losses. Amortisation is charged to the income statement on a straight line basis over the estimated useful life of the relevant asset. The estimated useful lives are specified as follows:

Software	3 years
Customer relations	7-10 years
Favourable aircraft lease contracts	2-3 years
Other intangible assets	6-10 years

(iii) *Subsequent expenditure*

Subsequent expenditure on capitalised intangible assets is capitalised only when it increases the future economic benefits embodied in the specific asset to which it relates. All other expenditure is expensed as incurred.

d. ***Operating income***

(i) *Transport revenue*

Passenger ticket sales are not recognised as revenue until transportation has been provided. Sold documents not used within nine months from the month of sale are recognised as revenue. Revenue from mail and cargo transportation is recognised in the income statement after transportation has been provided.

(ii) *Aircraft and aircrew lease*

Revenue from aircraft and aircrew lease is recognised in the income statement at the end of each charter flight.

(iii) *Other operating revenue*

Revenue from other services rendered is recognised in the income statement after the service has been provided.

Gain on sale of operating assets is recognised in the income statement after the risks and rewards of ownership have been transferred to the buyer.

Segment reporting

6. Segment information is presented in the consolidated financial statements based on matrix presentation, which includes business and geographical segments. The segment reporting reflects the Group's management and internal reporting structure and is devided into three segments. Investment activities comprise the operations of the parent. The second segment comprises the domestic aviation and tourism services operated in Icelandair Group hf. and its subsidiaries (discontinued) and Kynnisferðir ehf. (disposal group). The third segment comprises the operations of Sterling, Denmark (discontinued), a low fare airline.

   Inter-segment pricing is determined on an arm's length basis.

   Segment results include items directly attributable to a segment as well as those that can be allocated on a reasonable basis.

	Investment activities		**Iceland** Aviation and tourism services (Discontinued)		**Denmark** Aviation services (Discontinued)		Eliminations		Consolidated	
	2006	2005	2006	2005	2006	2005	2006	2005	2006	2005
Investment income	43,191	19,794	14	(204)	(240)	0			42,965	19,590
Operating income		232	45,088	47,412	48,275	0			93,363	47,644
Operating expenses without depreciation ..	(2,772)	(1,652)	(39,224)	(42,631)	(49,636)	0			(91,632)	(44,283)
Depreciation .... and amortisation	(24)	0	(1,977)	(2,408)	(767)	0			(2,768)	(2,408)
Segment result before .. income tax	40,395	18,374	3,901	2,169	(2,368)	0	0	0	41,928	20,543
Income tax	2,633	(2,969)	(667)	(323)	665	0			2,631	(3,292)
Profit for the year	43,028	15,405	3,234	1,846	(1,703)	0	0	0	44,559	17,251
Segment assets	262,226	106,524	904	37,837	0	0	(259)	(11,743)	262,871	132,618
Segment liabilities	119,562	32,093	634	30,835	0	0	0	4,753	120,195	58,175

Amounts are in ISK million

Discontinued operations

7. FL GROUP hf. sold its shares in Ferðaskrifstofa Íslands hf. and Bílaleiga Flugleiða ehf. in the beginning of the year 2006. The operations of these companies are therefore not part of the consolidated income statement for the year 2006.

In October 2006 FL GROUP hf. sold all its shares in Icelandair Group hf. for a selling price of ISK 33.5 billion. The income statement of Icelandair Group hf. is therefore not part of the consolidated income statement for the last quarter and the entity is not part of the consolidated balance sheet at year end.

At the end of December 2006, FL GROUP hf. sold all its shares in Sterling and related companies, which were acquired in the beginning of the year. Sterling´s operations were included in the consolidated income statement for the whole year 2006. Disclosures related to the acquisition of Sterling are made in note 9.

Profit from the discontinued operations specifies as follows:

	2006	2005
Results of discontinued operations:		
Revenue	93,363	47,412
Expenses	(91,604)	(45,039)
Results from operating activities	1,759	2,373
Net finance expense	(226)	(204)
Income tax expense	(2)	(323)
Results from operating activities, net of income tax	1,531	1,846
Gain on sale of discontinued operations	25,677	0
Profit for the year	27,208	1,846
Basic earnings per share	4.06	0.63
Diluted earnings per share	4.03	0.62
Cash flows from discontinued operations:		
Net cash from operating activities	1,982	3,981
Net cash from investing activities	2,822	30,799
Net cash used in financing activities	(584)	(30,188)
Net cash from discontinued operations	4,220	4,592

Effect of disposal on the financial position of the Group:

Cash and cash equivalents	7,065
Securities	5,289
Restricted cash	568
Loans, trade and other receivables	12,173
Inventories	1,560
Tax assets	1,653
Prepaid aircraft acquisitions	10,054
Operating assets	22,962
Intangible assets	21,694
Total assets	83,018

Amounts are in ISK million

7. Contd.:

Trade and other payables	12,637
Deferred income	9,394
Deferred income tax liability	996
Borrowings	34,344
Total liabilities	57,371
Net assets and liabilities	25,647
Consideration received:	
In cash	36,369
In debt securities	14,955
	51,324
Cash disposed of	7,065
Net cash inflow	29,304

Assets and liabilities held for sale

8. Kynnisferðir ehf., a subsidiary operating in the tourism industry, is presented as of 31 December 2006 as a disposal group held for sale following the commitment of the Group´s management to sell the company. Efforts to sell the company have commenced and it is expected to be sold during the year 2007.

Assets	
Cash and cash equivalents	50
Trade and other receivables	172
Investments in companies	15
Inventories	12
Operating assets	606
Intangible assets	49
Total assets classified as held for sale	904
Liabilities	
Trade and other payables	132
Deferred income tax liability	10
Borrowings	492
Total liabilities classified as held for sale	634

Business combination

9. At the end of October 2005 the Company entered into a contract regarding the acquisition of all outstanding shares in Sterling Airlines A/S, Flyselskabet af 15. Juli 2005 A/S and Sterling Icelandic ApS (together referred to as "Sterling"). FL GROUP hf. took over the operations of the company on 6 January 2006 when the conditions in the acquisition agreement were fulfilled.

Comparative amounts in the consolidated financial statements do not contain amounts from the financial statements of Sterling.

Amounts are in ISK million

9. Contd.:

The acquisition, accounted for according to the purchase method, had the following effect on the Group's balance sheet:

Cash and cash equivalents	1,660
Restricted cash	698
Trade and other receivables	3,457
Tax assets	751
Operating assets	2,410
Intangible assets	167
Trade and other payables	(5,514)
Deferred income	(4,148)
Borrowings	(2,275)
Net identifiable assets and liabilities, negative	(2,794)
Goodwill on acquisition	17,875
Consideration paid	15,081
Consideration satisfied by share issue	(4,022)
Consideration satisfied in cash	11,059
Net cash acquired	(1,660)
Acquisition of subsidiary, net of cash acquired according to the statement of cash flows	9,399

Purchase price allocations were not finalised during the year 2006 since the Company was sold before year end as disclosed in note 7. This has no impact on the Groups results in the consolidated income statement because of the sale. The goodwill recognised on the acquisition was attributable mainly to the work force and the synergies expected to be achieved from integrating the company into the Group’s existing aviation activities.

Sterling´s operations for the whole year 2006 are part of the consolidated income statement of FL GROUP hf.

Investment income

10. Net income from securities and derivatives is specified as follows:

	2006	2005
Gain on the sale of shares	15,145	1,473
Change in fair value of securities	10,200	13,748
Change in fair value of derivatives	(1,389)	6,737
Net income from securities and derivatives	23,956	21,958

Operating expenses

11. Operating expenses specify as follows:

Salaries, salary-related expenses and other personnel expenses, note 12	1,652	1,483
Depreciation	23	0
Other operating expenses	1,096	169
Total operating expenses	2,771	1,652

Amounts are in ISK million

Salaries and related expenses

12. Salaries and related expenses for the investment activities are specified as follows:

	2006	2005
Salaries and performance-based payments	1,071	1,027
Equity-settled shared-based payment transactions	435	68
Salary-related expenses	126	157
Total salaries and salary-related expenses	1,632	1,252
Other personnel expenses	20	231
Salaries, salary-related expenses and other personnel expenses, total	1,652	1,483
Average number of employees during the year	20	11

Auditors' fees

13. Remuneration to the Group's Auditors are specified as follows:

Audit of Financial Statements	33	18
Review of Interim Financial Statements	8	15
Other services	32	19
Total auditors' fees	73	52

The above mentioned figures include fees to the auditors of all companies within the Group during the year. Fees to other auditors than the auditors of the Parent Company amounted to ISK 17 million during the year 2006 (2005: ISK 11 million).

Income tax expense

14. Income tax recognised in the income statement is specified as follows:

Current tax	782	0
Origination and reversal of temporary differences	(3,413)	3,292
Total income tax expense in income statement	(2,631)	3,292

15. Reconciliation of effective tax rate:

		2006		2005
Profit before income tax		41,928		20,543
Income tax using the Company's domestic tax rate	18.0%	7,547	18.0%	3,697
Tax exempt revenue	(0.9%)	(390)	(0.2%)	(48)
Effect of tax rates in foreign jurisdictions	(0.1%)	(33)		
Tax incentives	(22.6%)	(9,485)		
Non-deductible expenses	0.0%	2	0.1%	25
Deferred tax assets of subsidiaries, previously not capitalised			(0.9%)	(193)
Other items	(0.9%)	(272)	(0.9%)	(189)
Effective tax rate	(6.3%)	(2,631)	16.0%	3,292

Amounts are in ISK million

Notes, contd.:

16. Income tax recognised directly in equity is specified as follows:

	2006	2005
Income tax on expense recognised directly in equity	34	2,240
Income tax related to excercised share based options to employees	0	168
Total income tax recognised directly in equity	34	2,408

Earnings per share

17. **Profit attributable to ordinary equity holders of the parent company:**

	2006	2005
Continuing operations	17,351	15,405
Discontinued operations	27,209	1,844
Total	44,560	17,249

Weighted average number of ordinary shares
in million shares

	2006	2005
Issued ordinary shares at 1 January	5,802	2,525
Effect of bought and sold own shares	(133)	(9)
Effect of the increase of share capital in November 2005	0	408
Effect of the increase of share capital in January 2006	284	0
Effect of the increase of share capital in July 2006	752	0
Weighted average number of ordinary shares at 31 December	6,705	2,924

Weighted average number of ordinary shares (diluted)
in million shares

	2006	2005
Weighted average number of ordinary shares (basic)	6,705	2,924
Effect of share options	49	29
Weighted average number of ordinary shares (diluted) at 31 December	6,754	2,953

Earnings per share:

	2006	2005
Basic earnings per share (ISK)	6.65	5.90
Diluted earnings per share (ISK)	6.60	5.84

Earnings per share from continuing operations:

	2006	2005
Basic earnings per share (ISK)	2.59	5.27
Diluted earnings per share (ISK)	2.57	5.22

Cash and cash equivalents

18. Cash and cash equivalents are specified as follows:

	2006	2005
Cash	6,786	8,850
Bank deposits	27,057	0
Mutual-fund certificates	13,179	1,500
Total cash and cash equivalents	47,022	10,350

Securities

19. Securities are specified as follows:

	Ownership	Fair value including related derivatives
Listed securities:		
Listed on the Icelandic Stock Exchange:		
Glitnir Bank hf.	30.36%	100,892
Other companies		50,410
Total listed on the Iceland Stock Exchange		151,302
Listed on foreign stock exchanges:		
AMR Corporation	6.00%	27,626
Finnair Oyj	22.42%	23,126
Bang & Olufsen A/S	11.45%	11,834
Royal Unibrew A/S	24.38%	14,013
Aktiv Kapital ASA	13.27%	6,671
Other companies		9,848
Total listed on foreign stock exchanges		93,118
Listed bonds:		
Listed bonds		8,729
Total listed securities		253,149
Unlisted securities:		
Refresco Holding B.V.	49.00%	
Northern Travel Holding ehf.	34.78%	
Highland Group Holding Limited	13.89%	
Mutual-fund certificates		
Other companies		
Total unlisted securities		14,819
Total securities		267,968
Thereof derivatives		(86,807)
Fair value of securities at year end		181,161

Associates

20. As presented in note 19, investments in associates are accounted for at fair value through profit or loss and presented within securities in the balance sheet. At year end 2006, based on both direct and indirect ownership, the following investments are defined as associates:

	Ownership
Finnair Oyj, Finland	22.42%
Glitnir Bank hf., Iceland	30.36%
Northern Travel Holding hf., Iceland	34.78%
Refresco Holding B.V., Holland	49.00%
Royal Unibrew A/S, Denmark	24.38%
Unity Investment ehf., Iceland	37.50%
Wyndeham Press Group Limited, United Kingdom	49.00%

Amounts are in ISK million

Derivatives

21. Net assets in derivatives are specified as follows:

	2006	2005
Equity derivatives - receivable, see note 19	86,807	45,336
Equity derivatives - payable	(86,169)	(40,377)
Net position of equity derivatives	638	4,959
Net position of other derivatives	(3,350)	1,105
Net position of derivatives	(2,712)	6,064
Derivatives - assets in the balance sheet	4,309	6,341
Derivatives - liabilities in the balance sheet	(7,021)	(277)
Net position of derivatives	(2,712)	6,064

Restricted cash

22. Bank deposits amounting to ISK 9,572 million are restricted to use for the Group at year end. These deposits are cash held by financial institutions as collaterals for derivative transactions.

Loans, trade and other receivables

23. Loans, trade and other receivables are specified as follows:

Loans, average effective interests 12.4%	14,830	1,442
Trade receivables	3,966	4,392
Prepaid expenses	380	350
Other receivables	302	1,273
Allowance account for impairment	0	(235)
Total loans, trade and other receivables	19,478	7,222

At 31 of December 2006 no allowance was conseded for doubtful receivables. No impairment loss was recognised during the year 2006.

24. Repayments of loans, trade and other receivables are specified as follows:

Repayments in 2007	6,966	7,222
Repayments in 2009	12,512	0
Total loans, trade and other receivables	19,478	7,222

Amounts are in ISK million

Operating assets

25. Operating assets are specified as follows:

Gross carrying amount	Buildings	Aircraft and flight equipment	Other operating assets	Total
Balance at 1.1.2005	3,323	22,507	3,826	29,656
Exchange rate difference	90	573	0	663
Additions through business combinations	0	1,992	27	2,019
Additions during the year	181	3,646	1,108	4,935
Sales and disposals during the year	(252)	(5,484)	(690)	(6,426)
Transferred to other items	0	(67)	(31)	(98)
Balance at 31.12.2005	3,342	23,167	4,240	30,749
Additions through business combinations	3,077	205	431	3,713
Additions during the year	114	11	674	799
Sales and disposals during the year	(6,385)	(23,383)	(3,813)	(33,581)
Transferred to other items	(148)	0	(1,083)	(1,231)
Balance 31.12.2006	0	0	449	449
Depreciation and impairment losses				
Balance at 1.1.2005	1,599	6,313	1,959	9,871
Exchange rate difference	44	122	0	166
Depreciation	116	1,605	519	2,240
Sales and disposals during the year	(87)	(1,685)	(475)	(2,247)
Transferred to other items	0	(12)	0	(12)
Balance 31.12.2005	1,672	6,343	2,003	10,018
Depreciation	203	18	191	412
Sales and disposals during the year	(1,861)	(6,361)	(1,559)	(9,781)
Transferred to other items	(14)	0	(611)	(625)
Balance 31.12.2006	0	0	24	24
Carrying amounts				
1.1.2005	1,724	16,194	1,867	19,785
31.12.2005	1,670	16,824	2,237	20,731
31.12.2006	0	0	425	425
Depreciation ratios	2-4%	4-10%	5-33%	

Intangible assets

26. The Group's intangible assets are specified as follows:

Gross carrying amount	Goodwill	Other intangible assets	Total
Balance at 1 January 2005	0	446	446
Additions	3,267	113	3,380
Sales and disposals during the year	0	(29)	(29)
Balance at 31 December 2005	3,267	530	3,797
Exchange rate difference	4,922	0	4,922
Additions during the year	18,016	0	18,016
Sales and disposals during the year	(26,156)	(530)	(26,686)
Transferred to other items	(49)	0	(49)
Balance at 31 December 2006	0	0	0

Amounts are in ISK million

26. Contd.:

Amortisation and impairment losses

	Goodwill	Other intangible assets	Total
Balance at 1 January 2005	0	162	162
Amortisation	0	168	168
Sales and disposals during the year	0	(3)	(3)
Balance 31.12.2005	0	327	327
Sales and disposals during the year	0	(327)	(327)
Balance at 31 December 2006	0	0	0

Carrying amounts

	Goodwill	Other intangible assets	Total
1.1.2005	0	284	284
31.12.2005	3,267	203	3,470
31.12.2006	0	0	0

Equity

27. ***Issued capital***

A shareholders meeting in January 2006 approved an increase in nominal value of share capital of ISK 296 million which was sold for ISK 4,022 million. The increase was part of the consideration paid for Sterling. In July 2006 a shareholders meeting approved to issue share capital amounting to nominal value of ISK 1,804 million which was sold for ISK 28,322 million. The increase was part of consideration paid in relation to acquisition of 24% stake in Straumur-Burðarás Investment Bank hf.

At 31 December 2006, the Board of Directors are allowed to increase the share capital by up to ISK 999 million during the next four years. Thereof ISK 692 million can be sold without the pre-emptory purchase provisions.

The Company's share capital, according to its Articles of Association amounts to ISK 7,945 million. The holders of ordinary shares are entitled to dividends as declared from time to time and are entitled to one vote per share at meetings of the Company. Share capital was increased during the year 2006 by a nominal value of ISK 2,100 million, from ISK 5,845 million to ISK 7,945 million. The Company bought own shares at a nominal value of ISK 657 million during the year for ISK 14,598 million. The Company sold own shares with a nominal value of ISK 518 million for ISK 11,479 million. Share capital according to the balance sheet amounted to ISK 7,763 million at the end of the year, share capital is specified as follows:

	Amounts	Ratio
Total issued shares at the end of the year	7,763	97.7%
Own shares	182	2.3%
Share capital according to the Articles of Association	7,945	100.0%

Amounts are in ISK million

27. Contd.:

Share premium

Share premium represents excess of payment above nominal value (ISK 1 per share) that shareholders have paid for shares sold by the Company. According to Icelandic Companies Act, 25% of the nominal value of share capital must be held in reserve which can not be paid out as dividend to shareholders.

Share option reserve

The reserve includes the accrued part of the fair value of share options. This reserve is reversed if share options are exercised or forfeited.

Hedging reserve

The hedging reserve comprised the effective portion of the cumulative net change in the fair value of cash flow hedging instruments related to hedged transactions that have not yet occurred. Hedge accounting was only applied in Icelandair Group hf. and at the disposal of the company the hedge reserve at Group level was transferred to the income statement.

Translation reserve

Foreign exchange differences arising on translation of financial statements of subsidiaries are recognised directly in a separate component of equity. When a foreign operation is disposed of, in part or in full, the relevant amount in the translation reserve is transferred to profit or loss.

Trade and other payables

28. Trade and other payables are specified as follows:

	2006	2005
Trade payables	2,410	3,532
Other payables	3,498	7,363
Total trade and other payables	5,908	10,895

Borrowings

29. Borrowings are specified as follows:

	Currency	Year of maturity	2006 Nominal value	2006 Carrying amount	2005 Carrying amount
Bank loan	ISK	2007-2012	39,640	39,987	12,589
Bank loan	EUR	2007-2009	42,266	41,762	240
Bank loan	DKK	2007	1,231	1,231	0
Bank loan	NOK	2007	1,048	1,048	0
Bank loan	USD	2007	20,927	20,927	26,701
Other currencies					138
Borrowings				104,955	39,668
Weighted average interest			8.27%		5.13%

Group's assets amounting to ISK 163,301 millions are mortgaged to secure derivative contracts and debt with the remaining balance of ISK 79,969 million at the end of the year 2006.

30. Repayment of borrowings are specified as follows:

	2006	2005
Repayments in 2006		23,699
Repayments in 2007	43,838	5,819
Repayments in 2008	0	3,080
Repayments in 2009	50,144	1,502
Repayments in 2010	0	2,295
Repayments in 2011	0	3,273
Subsequent repayments	10,973	0
Borrowings	104,955	39,668

Deferred income tax liability

31. The deferred income tax liability is specified as follows:

Deferred income tax liability 1.1.	4,694	1,451
Additions through business combination	0	77
Exchange rate difference	0	2,282
Income tax expense recognised in income statement	(3,413)	3,292
Income tax recognised in equity	(34)	(2,408)
Disposals during the year	(352)	0
Deferred income tax liability 31.12.	895	4,694

Amounts are in ISK million

31. Contd.:

The deferred income tax liability is attributable to the following items:

	2006	2005
Securities	22	3,766
Trade receivables	(266)	361
Operating assets	1,310	1,312
Other balance sheet items	(171)	(280)
	895	5,159
Tax losses carried forward	0	(465)
Deferred income tax liability 31.12.	895	4,694

	Assets		Liabilities		Net deferred tax liability	
	2006	2005	2006	2005	2006	2005
Securities			23	3,766	23	3,766
Trade receivables	(267)			361	(267)	361
Operating assets			1,310	1,312	1,310	1,312
Tax loss carry-forwards		(465)			0	(465)
Other items	(171)	(280)			(171)	(280)
	(438)	(745)	1,333	5,439	895	4,694

	1 January	Disposals during the year	Recognised in profit and loss	Recognised in equity	31 December
Securities	3,766		(3,743)		23
Trade receivables	361		(628)		(267)
Operating assets	1,312	(352)	351		1,311
Tax loss carry-forwards	(465)		465		0
Other items	(280)		142	(34)	(172)
	4,694	(352)	(3,413)	(34)	895

At 31 December 2006 deferred tax liability amounting to ISK 9,485 millions is not recognised for temporary differences of ISK 52,694 million related to an investment in subsidiaries because the Company controls whether the liability will be incurred and it is satisfied that it will not be incurred in the foreseeable future.

When the Group pays dividends to its shareholders, it is required to pay a portion of the dividends to taxation authorities on behalf of shareholders, i.e. withholding tax. The amount paid to taxation authorities is charged to equity as a part of the dividends.

Amounts are in ISK million

Share-based payments

32. The terms and conditions of grants are as follows:

Grant date / employees entitled	Number of instruments in thousands	Vesting conditions	Contractual life of option
Options granted 2005	130,500	12/24/36 months service	3 years
Options granted 2006	120,460	12/24/36 months service	3 years
Total	250,960		

All options are to be settled by physical delivery of shares. Options vesting in 12 months can be excercised three times during the contractual life, at the end of each 12 month period. Accordingly 24 month options can be exercised two times and the 36 month options only once at the end of the 36 month period.

The number and weighted average excercise price of share options is as follows in thousands:

	Weighted average exercise price 2006	Number of options 2006	Weighted average exercise price 2005	Number of options 2005
Outstanding at 1 January	13.6	217,650		
Forfeited during the year	13.6	(46,100)		
Exercised during the year	13.6	(41,050)		
Granted during the year	20.4	120,460	13.6	60
Outstanding at 31 December	16.9	250,960	13.6	60
Excercisable at 31 December		43,500		0

Options excercised during the year belong to key management of former subsidary, Icelandair Group hf. When Icelandair Group hf. was sold out of the Group, the remaing of options to the key management of Icelandair Group hf. were forfeited.

The options outstanding at 31 December 2006 have an exercise price in the range of 13.6 to 24.0 and a weighted average contractual life of 1.7 years. The share price at the date of exercise for share options exercised in 2006 was 23.1.

32. Contd.:

The fair value of services received in return for share options granted based on the fair value of share options granted, mesuring using a Black-Scholes model, with the following inputs:

	Granted 2005	Granted 2006
Fair value at grant date, average 12, 24, and 36 months options	3.63	5.76
Share price	13.6	20.4
Exercise price *	13.6	20.4
Expected volatility (weighted average volatility)	35.0%	35.0%
Option life (expected weighted average life)	2	2
Expected dividends *	0.0%	0.0%
Risk-free interest rate (based on government bonds)	9.4%	11.7%

* Excercise price is depended on dividends paid during the life of the option.

Total recognised expenses for the year arising from share-based payment transactions amounted to ISK 435 million (2005: ISK 68 million) including forfeited options during the year and accrued social security expenses related to share-based payments.

Financial instruments and associated risks

33. The Group maintains positions in a variety of derivative and non-derivative financial instruments in accordance with its investment strategy. The Group´s investment portfolio comprises quoted and non-quoted equity and debt investments.

The Group's investing activities expose it to various types of risk that are associated with the financial instruments and markets in which it invests. The most important types of financial risk to which the Group is exposed are market risk, credit risk and liquidity risk.

The frame for asset allocation is determined by the Group´s Investment Committee who sets the outline for the distribution of the assets to achieve the investment objectives. Divergence from target asset allocations and the composition of the portfolio is monitored on intraday bases by the Group´s employees.

The nature and extent of the financial instruments outstanding at the reporting date and the risk management policies employed by the Group are discussed below.

Market risk

Market risk embodies the potential for both loss and gains and includes currency risk, interest rate risk and price risk.

The Group's strategy on the management of market risk is driven by the Group's investment objective. The Group's market risk is managed on a daily basis by the employees in accordance with policies and procedures in place. The Group's overall market positions are monitored on a monthly basis, or in some cases more frequently, by the board of directors.

Details of the Group's investment portfolio at the reporting date are disclosed in the schedule of investments included in note 19.

Amounts are in ISK million

33. Contd.:

Currency risk
The Group entities may invest in financial instruments and enter into transactions denominated in currencies other than its functional currency. Consequently, the Group is exposed to risks that the exchange rate of its currency relative to foreign currencies may change in a manner that has an adverse affect on the value of that portion of the Group's assets or liabilities denominated in currencies other than the Icelandic kronas (ISK).

The Group's total net currency balance is monitored on daily basis and traded as any other calculated financial position.

Interest rate risk
The majority of the Group's financial assets are non-interest-bearing. Interest-bearing financial assets reprice in the short-term, no longer than twelve months. As a result, the Group is subject to limited exposure to fair value interest rate risk due to fluctuations in the prevailing levels of market interest rates when it comes to assets. The Group is however exposed to interest risk from interest bearing liabilities and that risk is mitigated by active risk management. Any excess cash and cash equivalents of the Group are invested in short-term commercial paper or reverse repurchase agreements with the term to maturity no longer than one month.

Price risk
Price risk is the risk that value of the instrument will fluctuate as a result of changes in market prices, whether caused by factors specific to an individual investment, its issuer or all factors affecting all instruments traded in the market.

As the majority of the Group´s financial assets are carried at fair value with fair value changes recognised in the income statement, all changes in market conditions will directly affect investment income.

Price risk is mitigated by the Group´s Management by constructing a diversified portfolio of investments and instruments traded on various markets. In addition market fluctuations are monitored on intraday basis which enables the company to react quickly to any changes in the market.

The Group´s financial investments is diversified by industries as follows:

	2006	2005
Banks / Financial Services	52.9%	66.4%
Aviation	21.5%	22.0%
Consumer and retail	9.3%	2.9%
Beverage	7.4%	0.0%
Other	8.9%	8.7%

Credit risk

Credit risk is the risk that a counterparty to a financial instrument will fail to discharge an obligation or commitment that it has entered into with the Group. The Group´s management looks to minimize this risk factor by only entering agreements with solid and well known institutions in addition to closely monitoring the credit risk on an ongoing basis.

Amounts are in ISK million

33. Contd.:

Transactions involving derivative financial instruments are usually with counterparties with whom the Group has signed master netting agreements. Master netting agreements provide for the net settlement of contracts with the same counterparty in the event of default. The impact of the master netting agreements is to reduce credit risk.

There were no significant concentrations of credit risk to counterparties at 31 December 2006.

Liquidity risk

The Group´s financial instruments can include investments in unlisted equity investments and derivative contracts traded over-the-counter, which are not traded in an organised public market and which generally may be illiquid. As a result, the Group may not be able to liquidate quickly some of its investments in these instruments at an amount close to its fair value in order to meet its liquidity requirements, or to respond to specific events such as a deterioration in the credit-worthiness of any particular issuer.

To mitigate this risk the company has a policy of minimum available cash at any given time and in addition to that, the Group´s listed financial investments, which represent large part of the total assets, are considered to be readily realisable as they are all listed on stock exchanges.

Financial instruments and fair values

34. The fair values of financial assets and liabilities is not significantly different than the carrying amounts shown in the balance sheet.

Financial Guarantees

35. The Company is still bound to certain guarantees provided in favour of Sterling's creditors. As a part of the sale of Sterling, the buyer committed to release the aforementioned guarantees provided by the Company to Sterling´s creditors within 12 months from closing (completion of the sale and purchase). These guarantees amounted to ISK 7,737 million at the acquistion date. The Company receives arm´s lenght fees for providing the aforementioned guarantees.

The Company is still bound to certain gurantees provided in favour of Icelandair Group hf.

With regards to agreements on financing of three aircrafts the Company guarantees loans amounting to ISK 5 billion while transfer of obligations takes place. The Company receives guarantee fees for these obligations on a step-up basis from 0.5%-3.0% depending on time length.

The Company also guarantees aircraft financing amounting to ISK 4 billion until 15 April 2006 and pre-delivery payments made in relation to acquistion of aircrafts amounting to ISK 8 billion for a 12 month period. Furthermore, the Company guarantees operating lease payments for a 12 month period, monthly lease payments amount to ISK 25 million.

In relation to the above mentioned guarantees provided in favour of creditors of Icelandair Group hf. the buyer of Icelandair Group hf. has committed to hold the Company harmless in relation to any claims or cost deriving from the aforementioned guarantees.

Related parties

Identity of related parties

36. The Group has a related party relationship with its subsidiaries, associates, and with its directors and executive officers.

Transactions with management and key personnel

Salaries and benefits of management paid for their work for Group companies, share option agreements and shares in the Company are specified as follows:

	Salaries and benefits	Share options	Share held at year-end 2006
Board of Directors:			
Skarphéðinn Berg Steinarsson, Chairman of the Board	4.0		0.7
Jón Ásgeir Jóhannesson	2.9		
Kristinn Björnsson	1.5		2.0
Magnús Ármann	2.9		
Paul Davidson	2.9		
Smári S. Sigurðsson	2.9		
Þorsteinn M. Jónsson	2.9		
Peter Mollerup, alternative board member	1.4		
Þórður Bogason, former alternative board member	0.2		
Kristinn Bjarnason, former alternative board member	0.1		
Managing directors:			
Hannes Smárason, CEO	51.0		1,570.4
Jón Sigurðsson, Deputy CEO	86.4	51.5	
Three directors of the Parent Company	145.8	85.0	

Included in the above mentioned list of shares held by management and directors are shares held by companies controlled by them and derivative agreements entered into regarding shares in the Company.

Other transactions with related parties

During the year 2006 the Group made transactions with related parties. These transactions were priced on an arm's length basis. Outstanding loans and receivables at year end amounted to ISK 16.648 million.

Amounts are in ISK million

36. Contd.:

Group entities

The Company holds seven subsidiaries which all are included in the consolidated financial statements. The direct subsidiaries included in the consolidated financial statements are specified as follows:

	Share 31/12/2006
Investments:	
FL Group Danmark ApS	100%
FL Group UK limited	100%
FL Trading AS	100%
FL Holding Netherlands B.V.	100%
FL GLB Holding B.V.	100%
Tónvís ehf.	100%
Disposal Group:	
Kynnisferðir ehf.	96%

FL Investment ehf., a 100% owned subsidiary at year-end 2005, was merged with the Parent Company as of 1 January 2006.

The subsidiaries own five subsidiaries that are included in the consolidated financial statements. These subsidiaries have immaterial effects on the accounts.

Amounts are in ISK million