PROSPECTUS
FEBRUARY 2007

ICELANDAIR GROUP HF.

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This Prospectus is published on 12 February 2007.

The Prospectus has been scrutinised and approved by the Iceland Stock Exchange (ICEX) on behalf of the Financial Service Authority in Iceland. It was prepared for the listing of Icelandair Group hf. on the ICEX Main List.

This Prospectus, published in English only, consists of three documents: Summary, Securities Note and Registration Document.

For the timeframe of 12 months from the date of the Prospectus (lifetime of the document), the Prospectus is available on the website: www.icelandairgroup.is.

I.
SUMMARY

This summary should be read as an introduction to the Prospectus dated 12 February 2007 containing this Summary, a Securities Note and a Registration Document. Prospective investors should read the Prospectus in its entirety. Because this is a summary, it does not contain all the information that may be important to you. You should read this summary in conjunction with the more detailed information in the rest of the Prospectus, including the "Risk Factors" sections and the financial statements and the notes thereto. Any decision to invest in the Shares should be based on consideration of the Prospectus as a whole.

Following the implementation of the relevant provisions of the Prospectus Directive in each member state of the European Economic Area, no civil liability will attach to us or our board of directors in any such member state in respect of this summary, including any translation hereof, unless it is misleading, inaccurate or inconsistent when read together with the other parts of the Prospectus. Where a claim relating to the information contained in the Prospectus is brought before a court in a member state of the European Economic Area, the plaintiff investor may, under the national legislation of the member state where the claim is brought, be required to bear the costs of translating the Prospectus before the legal proceedings are initiated.

LISTING ON ICEX MAIN LIST

This Summary concerns the listing of all 1,000,000,000 issued shares in Icelandair Group hf. on the Iceland Stock Exchange (ICEX) Main List. The ISIN number of the shares is IS0000013464.

ICELANDAIR GROUP

Icelandair Group hf., Icelandic ID-No. 631205-1780, Reykjavík Airport, 101 Reykjavík, Iceland, telephone number +354 505 0300.

GLITNIR BANKI HF. (LISTING ADVISOR)

Glitnir banki hf., Icelandic ID No. 550500-3530, Kirkjusandi 2, 155 Reykjavík, telephone number: +354 440 4000.

RISK FACTORS

An investment in the shares of Icelandair Group involves risks, both general risks relating to investments in securities and risks relating to the operations of the Issuer. The risk should be assessed by potential investors before making an investment in the shares and investors are advised to study the discussion of risk in the Securities Note and the Registration Document thoroughly.

Examples of risk factors that may have a material effect on the price of the Issuer's shares, and thereby on the investment value, are market risk, liquidity risk and counterparty risk. The share price can fluctuate considerably due to factors such as variations in operating income or cost, changes in the market environment, adverse commentary about the Issuer and its operations and services in the media and changes to the Issuer's competitive position. The structure of shareholder ownership and the possibility of dilution of shares by new share issue can also be risk factor for investors.

Among the important risks to which Icelandair Group is directly exposed are risk factors relating to the Company as an airline operator, such as fuel price and availability, seasonality, airport access and security, increased competition and changes in regulations and applicable law. Strikes and the risk of key employees resigning could potentially have material effects on the Issuer. Tax issues, litigations, exchange rate and interest rate fluctuations and the coverage of insurance agreements are also potential risk factors worth consideration.

MARKET MAKING

According to two separate agreements, Glitnir banki hf. and Straumur Burðarás Investment Bank hf. will act as market makers for Icelandair Group hf.'s shares after the listing on ICEX Main List.

Glitnir banki hf. shall through its own account submit daily bids and asks to the ICEX for a minimum of ISK 15 million (purchasing price) on each side at a price determined by the market maker on any given occasion. The maximum bid/ask spread may not exceed 1.0% and the difference from the last price paid may not exceed 3.0%. The market maker is obliged to provide liquidity for up to ISK 150 million per day.

Straumur Burðarás Investment Bank hf. shall through its own account submit daily bids and asks to the ICEX for a minimum of ISK 13.5 million (purchasing price) each side at a price determined by the market maker on any given occasion. The maximum bid/ask spread may not exceed 1.0% and the difference from the last price paid may not exceed 3.0%. Straumur Burðarás Investment Bank hf. is obliged to provide liquidity for up to ISK 150 million per day.

COST OF THE LISTING

The total cost of the admission to trading of this share capital on the Main List of the ICEX is estimated at ISK 10 million, including charges from ICEX. All costs of the admission to trading will fall on the Company.

INFORMATION ON ICELANDAIR GROUP

HISTORY AND DEVELOPMENT

The history of Icelandair Group's predecessors dates back to 1937, almost as long as the history of commercial aviation in Iceland, which began in 1919, less than 16 years after the Wright brothers made the first ever powered flight. Icelandair Group predecessor, Flugleiðir hf., was established in Reykjavik on July 20, 1973, by a merger of Flugfélag Íslands hf. and Loftleiðir hf. Flugleiðir's main operations during the period 1937-2005 were in aviation. Flugleiðir was listed on the ICEX Main List in 1992.

At Flugleiðir's annual general meeting in 2005, the company's name was changed to FL Group and in October 2005, fundamental changes took place by which investment activities became FL Group's main focus. FL Group's acquisitions and corporations were divided into groups, Icelandair Group hf. being one of them and comprising Icelandair, Icelandair Technical Services, Icelandair Ground Services, Loftleiðir-Icelandic and Icelandair Cargo. In February 2006, the board of directors of FL Group announced its intention to list Icelandair Group hf. on the ICEX but postponed it because of unfavourable market conditions. At that time, Air Iceland, Iceland Travel and Icelandair Hotels were transferred to Icelandair Group hf. as were Bluebird Cargo, Icelandair Shared Services, Icelease, IG Invest and Icecap.

In October 2006 three qualified investors, Langflug ehf., Naust ehf. and Ómar Benediktsson founded Icelandair Group Holding hf. with the goal of purchasing Icelandair Group hf. and committed themselves to invest 50.5% of the equity in Icelandair Group Holding. At the same time, Glitnir banki hf. underwrote 49.5% of Icelandair Group Holding as a part of the transaction where Icelandair Group Holding hf. bought Icelandair Group hf. from FL Group. The underwritten shares were sold to groups of qualified investors in October 2006, except 18.5% which were sold, by Glitnir hf., via a share offer, from 27 November to 4 December 2006, to Icelandair Group employees, the general public and qualified investors. Following the share offer, Icelandair Group Holding was listed on the ICEX Main List on 14 December 2006.

On 29 December, 2006 the shareholders of Icelandair Group Holding hf. agreed to the merger of Icelandair Group Holding hf. and Icelandair Group hf. effective as of 1 November, 2006. Following the merger, Icelandair Group will be listed on the ICEX Main List on 12 February 2007 and Icelandair Group Holding delisted after closing on 9 February 2007.

BUSINESS OVERVIEW

Icelandair Group's purpose is to provide its shareholders with good return on their investment. This is done by owning and operating profitable and dynamic service and trade companies with strong growth potential in the airline, transportation and tourism industry.

The operation of Icelandair Group is divided into 13 subsidiaries. Each business is managed to create value through strategic and business development decisions. Two subsidiaries play a supporting role: Icelandair Shared Services and Icecap, an insurance company. The other subsidiaries are grouped into three focus areas: Scheduled Airline Operations, Global Capacity Solutions and Aircraft Trading and Travel and Tourism Infrastructure.

On 31 December 2006, the Company employed 2,747 people.

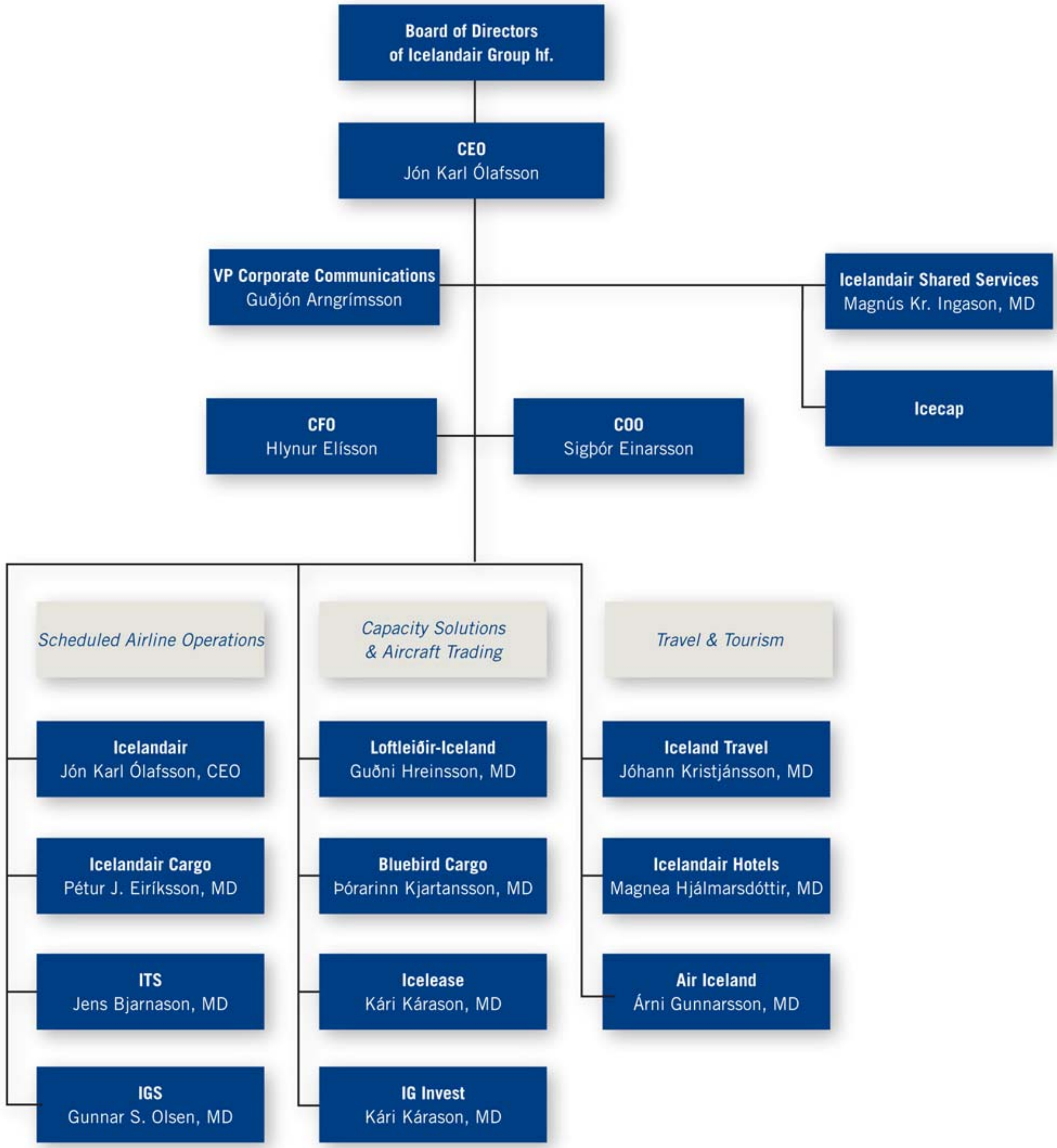

Figure 1. The organizational structure of Icelandair Group

SUMMARY

SECURITIES NOTE

REGISTRATION DOCUMENT

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BOARD OF DIRECTORS

The board of directors of Icelandair Group hf. has the supreme authority in the Issuer's general affairs between shareholders' meetings and endeavours to keep the organization and operations on course. The Issuer presently has 7 board members.

- Finnur Ingólfsson, chairman of the board of directors
- Ómar Benediktsson, vice chairman of the board of directors
- Hermann S. Guðmundsson, member of the board of directors
- Einar Sveinsson , member of the board of directors
- Marta Eiríksdóttir, member of the board of directors
- Helgi Sigurður Guðmundsson, member of the board of directors
- Jóhann Magnússon, member of the board of directors

SENIOR MANAGEMENT

The Senior Management team, under the leadership of the CEO, Jón Karl Ólafsson, comprises three managing directors.

- Jón Karl Ólafsson, CEO
- Hlynur Elísson, CFO
- Sigþór Einarsson, COO

STATUTORY AUDITORS

The registered auditor of Icelandair Group hf. is KPMG hf., Icelandic ID No. 590975-0449, Borgartún 27, IS-105 Reykjavík, Iceland. KPMG hf. has reviewed the consolidated pro forma income statement for 2005 for Icelandair Group, interim report for Icelandair Group for the first six months of 2006 and the opening pro forma balance sheet at 1 January for Icelandair Group. KPMG hf. has furthermore audited the interim report of Icelandair Group hf. dated 30 September 2006 and the annual accounts of Icelandair, Icelandair Cargo, Loftleiðir-Icelandic and Air Iceland for the years ended December 31, 2003, 2004 and 2005. KPMG has also audited the income statements, balance sheets and statements of cash flow for the first nine months of 2006 for Icelandair, Icelandair Cargo, Loftleiðir Icelandic, Bluebird Cargo and Air Iceland. In addition to this KPMG has compiled the interim consolidated balance sheet of Icelandair Group hf. and its subsidiaries as of 31 March 2006 and the related consolidated income statement and statement of cash flows for the three months then ended.

Grant Thornton endurskoðun ehf., Icelandic ID No. 430190-1999, Suðurlandsbraut 20, 108 Reykjavík, Iceland, has audited the financial information for Bluebird Cargo ehf. for the years ending December 31, 2003, 2004 and 2005. Grant Thornton confirms that all information in this Registration Document regarding financial information for Bluebird Cargo is consistent with the said financial statements it has audited.

LIST OF MAJOR SHAREHOLDERS

Table 1. The 20 largest shareholders of the Company as of 6 February 2007

Name	Share capital	Share capital
Langflug ehf	320,000,000	32.0%
Naust ehf	148,148,148	14.8%
Fjárfestingafélagið Máttur ehf	111,111,111	11.1%
GLB Hedge	78,300,867	7.8%
Urður ehf	55,555,556	5.6%
Glitnir banki hf	41,148,073	4.1%
Flugval ehf	18,518,519	1.9%
Lífeyrissjóðir Bankastræti 7	14,769,600	1.5%
Samvinnulífeyrissjóðurinn	12,887,666	1.3%
Lífeyrissjóður verslunarmanna	11,111,111	1.1%
Saxbygg ehf	10,000,000	1.0%
Miðbæjareignir ehf	10,000,000	1.0%
Magt ehf	9,259,260	0.9%
Credit Suisse Securities(Eu)Ltd	9,000,000	0.9%
Lífeyrissjóður Austurlands	8,650,000	0.9%
Almenni lífeyrissjóðurinn	8,006,047	0.8%
Gildi -lífeyrissjóður	7,230,290	0.7%
Barclays Capital Securities Ltd.	7,000,000	0.7%
Glitnir Sjóðir hf,sjóður 10	6,844,954	0.7%
Sameinaði lífeyrissjóðurinn	5,799,407	0.6%
	893,340,609	89.3%

RELATED PARTY TRANSACTIONS

The board of directors of the Company believes that the Company's related party transactions described below are conducted on an arm's length basis.

Attention is drawn to Icelandair ehf's. recent agreement with Olíufélagið ehf. regarding fuel services for Icelandair at Keflavík Airport. This agreement was reached after seeking offers from all major oil distributors in Iceland. The majority owner of Olíufélagið ehf. is BNT hf. which also owns 49.9% share in Naust ehf., one of Icelandair Group main shareholders. It is the management's opinion that this agreement was reached at fair value. The amount relating to this agreement represents approximately 6.5% of the Icelandair's revenue.

Icelandair Group hf. and its subsidiaries have insurance agreements with Sjóva hf., who is one of the owners of Fjárfestingafélagið Máttur ehf, which is a shareholder in the Company. However, the amount relating to this agreement is less than 0.05% of the Company's turnover in 2005.

No other material transactions have taken place with related parties.

BORROWING REQUIREMENTS AND FUNDING STRUCTURE

The company recently finalised the purchase of two 737-400 aircraft in connection with Bluebird Cargo's operations. The purchase price was ISK 2.2 billion and reservations amount to ISK 414 million. ISK 2.1 billion or 80% of this sum will be financed by new debt. Next year two aircraft will be sold to offset this investment. In December 2006 the company signed a letter of intent regarding the purchase of two Boeing 757-200 aircraft, which will, if the purchase will be finalized, result in increased borrowing requirements. Currently there are no other material borrowing requirements. Borrowings as of 31 October 2006 amounted to ISK 49,333 million. Of total borrowings ISK 23,706 million is secured. None of Icelandair Group's borrowing is guaranteed.

The following table shows the consolidated capitalization and indebtedness of Icelandair Group as of 31 October 2006 taking into account the Merger and increased indebtedness of Icelandair Group Holding following the purchase of Icelandair Group on 15 October 2006. The balance sheet was generated internally and has not been audited.

Table 2. The consolidated capitalization and indebtedness of the Company

Current liabilities			
Guaranteed	0		
Secured	12,506		
Unguaranteed/Unsecured	18,013	Cash and cash equivalents	4,490
Total current liabilities	30,519		
Non-current liabilities		Current financial receivables	6,345
Guaranteed	0		
Secured	11,200	Current bank debt	(3,600)
Unguaranteed/unsecured	7,614	Current portion of non current debt	(12,200)
Total non-current liabilities	18,814	Trade and other payables	(11,319)
		Other current finacial debt	(3,400)
Shareholders' equity		Current financial debt	(30,519)
Share capital	1,000		
Share premium	25,223	Non-current bank loans	(17,814)
Other reserve	834	Other non-current loans	(1,000)
Total equity	27,057	Non-current financial indebtedness	(18,814)
Total capitalisation	76,390	**Net financial indebtedness**	(38,498)

SELECTED FINANCIAL INFORMATION

Table 3. Key Figures for Icelandair for the period 2003-2005 and the first nine months of 2005 and 2006. Balance Sheet figures are for the end of each period. All figures in ISK million.

	2003	2004	2005	1/1-30/9 2005	1/1-30/9 2006
Profit and loss account					
Transport revenue	18,161	20,409	23,818	18,805	22,408
Aircraft and air crew lease	4,991	6,968	6,161	4,450	5,682
Other operating revenue	2,548	1,680	1,484	1,069	1,437
Operating expenses before depreciation	(24,900)	(27,981)	(30,483)	(22,975)	(26,406)
Depreciation	(125)	(691)	(684)	(528)	(949)
EBITDA	800	1,076	980	1,349	3,121
EBIT	675	385	296	821	2,172
Pre-tax profit	613	127	557	825	2,677
Income tax	(111)	(28)	(108)	(155)	(488)
Profit for the period	502	99	449	670	2,189
Balance Sheet					
Total assets	9,502	9,339	11,662		29,009
Liabilities	6,226	6,219	8,020		23,076
Equity capital	3,276	3,120	3,642		5,933
Cash flow					
From operating activities	3,831	1,464	2,781	3,502	5,082

Table 4. Key Figures for Icelandair Cargo for the period 2003-2005 and the first nine months of 2005 and 2006. Balance Sheet figures are for the end of each period. All figures in ISK million.

	2003	2004	2005	1/1-30/9 2005	1/1-30/9 2006
Profit and loss account					
Cargo and mail	2,698	3,207	3,053	2,203	2,923
Aircraft lease	436	442	282	166	710
Service revenue	759	1,096	1,213	876	1,126
Other operating revenue	23	27	34	20	40
Operating expenses before depreciation	(3,723)	(4,449)	(4,550)	(3,218)	(4,654)
Depreciation	(12)	(21)	(26)	(19)	(14)
EBITDA	193	323	32	46	145
EBIT	181	302	6	27	131
Pre-tax profit	219	301	9	25	146
Income tax	(1)	(55)	(2)	(5)	(28)
Profit for the period	218	246	7	20	118
Balance Sheet					
Total assets	877	958	1,014		1,237
Liabilities	762	604	882		989
Equity capital	115	354	133		248
Cash flow					
From operating activities	411	162	18	98	(2)

Table 5. Key Figures for Loftleiðir Icelandic for the period 2003-2005 and the first nine months of 2005 and 2006. Balance Sheet figures are for the end of each period. All figures in ISK million.

	2003	2004	2005	1/1-30/9 2005	1/1-30/9 2006
Profit and loss account					
Aircraft and air crew lease	3,902	5,454	5,573	4,161	4,947
Sale of assets	0	0	0	0	411
Other operating revenue	14	19	36	25	29
Operating expenses before depreciation	(4,160)	(5,365)	(5,248)	(3,895)	(5,093)
Depreciation	(2)	(5)	(4)	(3)	(15)
EBITDA	(244)	108	361	291	294
EBIT	(246)	103	357	288	280
Pre-tax profit	(231)	85	325	261	334
Income tax	73	(15)	(60)	(49)	(40)
Profit for the period	(158)	70	265	212	294
Balance Sheet					
Total assets	424	554	1,172		2,671
Liabilities	752	775	1,095		2,351
Equity capital	(328)	(221)	77		320
Cash flow					
From operating activities	58	292	522	429	31

Table 6. Key Figures for Bluebird Cargo for the period 2003-2005 and the first nine months of 2005 and 2006. Balance Sheet figures are for the end of each period. All figures in ISK million.

	2003	2004	2005	1/1-30/9 2005	1/1-30/9 2006
Profit and loss account					
Sales income	1,489	2,136	2,241	1,702	2,164
Other operating income	5	74	21	18	15
Operating expenses before depreciation	(920)	(1,500)	(1,766)	(1,359)	(1,632)
Depreciation	(251)	(269)	(223)	(186)	(193)
EBITDA	575	711	496	360	547
EBIT	324	441	273	175	354
Pre-tax profit	150	296	158	85	276
Income tax	(5)	(47)	(35)	(21)	(50)
Profit for the period	145	249	123	64	226
Balance Sheet					
Total assets	2,655	2,429	2,409		2,914
Liabilities	2,188	1,778	1,615		1,804
Equity capital	467	651	794		1,109
Cash flow					
From operating activities	407	468	438	295	570

Table 7. Key Figures for Air Iceland for the period 2003-2005 and the first nine months of 2005 and 2006. Balance Sheet figures are for the end of each period. All figures in ISK million.

	2003	2004	2005	1/1-30/9 2005	1/1-30/9 2006
Profit and loss account					
Transport revenue	1,972	2,259	2,591	1,885	2,355
Cargo and mail	105	97	103	76	111
Aircraft and air crew lease	408	520	498	415	413
Other operating revenue	438	465	358	337	327
Operating expenses before depreciation	(2,527)	(2,723)	(3,068)	(2,328)	(2,555)
Depreciation	(132)	(193)	(182)	(137)	(183)
EBITDA	397	618	483	384	650
EBIT	265	425	302	248	467
Pre-tax profit	227	384	247	214	403
Income tax	158	(70)	(46)	(39)	(74)
Profit for the period	385	314	201	175	329
Balance Sheet					
Total assets	1,552	1,813	1,218		3,576
Liabilities	687	978	537		2,565
Equity capital	866	835	681		1,011
Cash flow					
From operating activities	286	877	282	136	238

Table 8. Key figures for Icelandair Group the first three quarters of 2006 and combined for the first nine months of 2006. All figures in ISK million.

	Q1 2006 1/1-31/3	Q2 2006 1/4-30/6	Q3 2006 1/7-30/9	2006 1/1-30/9
Profit and loss account				
Transport revenue	5,555	9,613	12,480	27,648
Aircraft and air crew lease	2,217	2,268	3,290	7,775
Other operating revenue	1,823	2,600	3,707	8,130
Operating expenses before depreciation	(9,860)	(12,917)	(15,056)	(37,833)
Depreciation	(827)	(409)	(642)	(1,878)
EBITDAR	304	2,385	5,432	8,121
EBITDA	(265)	1,564	4,421	5,720
EBIT	(1,092)	1,155	3,779	3,842
Pre-tax profit	(677)	1,560	3,056	3,939
Income tax	122	(281)	(515)	(674)
Profit for the period	(555)	1,279	2,541	3,265
Balance Sheet				
Total assets				67,892
Liabilities				44,510
Equity capital				23,382
Cash flow				
From operating activities	979	3,857	1,557	6,393

FUTURE OUTLOOK

Icelandair Group hf. has set a goal for 5-7% annual internal growth, for the coming years, with hopes of even higher growth for 2006 and 2007. Additionally, the company does not rule out making acquisitions to bolster its operations.

Icelandair Group hf. has an objective to have its EBIT 5-7%, measured against total revenue. EBIT is defined as earnings before interest expense and taxes.

In order to secure the stability of the scheduled operation, Icelandair Group hf. strives to keep a reserve of no less than 10% of Icelandair's ehf. annual revenue. This reserve will be kept in a mix of cash and securities with a maturity less than 90 days. This reserve is estimated to be sufficient to meet a conceivable net cash outflow cased by a sudden shock in Icelandair's ehf. operations.

INVESTMENTS

Icelandair Group's investments are mainly due to investment in aircraft, flight equipment and aircraft engines. Table 9 lists the most significant investments for the past financial years.

Table 9. Icelandair Group Holding's investments in 2003-2006

Year	Investment	ISK millions	% of capex
2006	2 Boeing 737-400	2,200	39%
2006	Latcharter Airlines	507	9%
2006	2 Dash 8-100 aircraft	685	12%
2006	Boeing 757-200 winglets	280	5%
2006	Airline Services Estonia	104	2%
2006	Other	1,850	33%
2005	2 engines	400	20%
2005	Hotel Nordica	300	15%
2005	ITS spare parts	250	13%
2005	Other	1,244	63%
2004	3 F-50 aircraft	400	22%
2004	ITS spare parts	250	14%
2004	Hotel Nordica	120	7%
2004	Other	1,015	57%
2003	Hotel Nordica	600	25%
2003	ITS	600	25%
2003	Other	1,179	50%

DOCUMENTS ON DISPLAY

For the life of this Prospectus, published on 12 February 2007, the following documents may be inspected on Icelandair Group hf.'s registered office Reykjavik Airport, 101 Reykjavik, Iceland and on Icelandair Group hf.'s website http://www.icelandairgroup.is:

- The Registration Document, Security Note and Summary dated 9 February 2007.
- Icelandair Group hf.'s Articles of Association.
- Stock Option Plan for Key Employees of Icelandair Group hf. dated 29 December 2006.
- The consolidated balance sheet for Icelandair Group hf. dated 31 October 2006. The balance sheet is internally generated and has not been audited.
- Icelandair Group hf.'s reviewed consolidated pro forma income statements for the financial year ending 31 December 2005 (including the auditors' reports issued in respect thereof).
- Icelandair Group hf.'s reviewed consolidated pro forma opening balance sheet at 1 January 2006 (including the auditors' reports issued in respect thereof).
- Icelandair Group hf.'s interim report for the first three months of 2006, reviewed interim report for the six months ending 30 June 2006 and audited interim report for the nine months ending 30 September 2006.
- The audited annual financial statements for Icelandair, Icelandair Cargo, Loftleiðir-Icelandic, Bluebird Cargo and Air Iceland for each of the financial years ending 31 December 2003, 31 December 2004 and 31 December 2005 (including the audit reports issued in respect thereof).
- The audited interim income statements, balance sheets and cash flow statements for Icelandair, Icelandair Cargo, Loftleiðir-Icelandic, Bluebird Cargo and Air Iceland for the first nine months of 2006.
- The interim financial statement for Icelandair, Icelandair Cargo, Loftleiðir Icelandic, Bluebird Cargo and Air Iceland for the first nine months of 2005. These accounts have not been audited.
- The Merger plan for Icelandair Group Holding hf. and Icelandair Group hf. dated 15 November 2006.
- Assessors report on the merger of Icelandair Group Holding hf. and Icelandair Group hf.

DOCUMENTS INCORPORATED BY REFERENCE

For the life of this Prospectus, published on 12 February 2007, the following documents in the Registration Document for Icelandair Group Holding dated 26 November 2006 shall be deemed to be incorporated in, and to form part of this Registration Document. The non-incorporated parts of the Registration Document for Icelandair Group Holding are either not relevant for the investor or covered elsewhere in this Prospectus. Icelandair Group Holding has been merged with Icelandair Group and all information relevant to the merged company are contained in this Prospectus.

- In section 28.1 merger plan for Icelandair Group Golding hf. and Icelandair Group hf. and KPMG report on the merger of Icelandair Group Holding hf. and Icelandair Group hf.
- In section 28.3 financial reports for Icelandair ehf.
  - In section 28.3.1 audited 2003 – 2005 annual reports
  - In section 28.3.2 interim income statement, balance sheet and cash flow statement for the nine month period ending 30 September 2005
  - In section 28.3.3 audited interim income statement, balance sheet and cash flow statement for the nine month period ending 30 September 2006
- In section 28.4 financial reports for Flugleiðir frakt ehf. (Icelandair Cargo)
  - In section 28.4.1 audited 2003 – 2005 annual reports
  - In section 28.4.2 interim income statement, balance sheet and cash flow statement for the nine month period ending 30 September 2005
  - In section 28.4.3 audited interim income statement, balance sheet and cash flow statement for the nine month period ending 30 September 2006
- In section 28.5 financial reports for Loftleiðir-Icelandic ehf.
  - In section 28.5.1 audited 2003 – 2005 annual reports
  - In section 28.5.2 interim income statement, balance sheet and cash flow statement for the nine month period ending 30 September 2005
  - In section 28.5.3 audited interim income statement, balance sheet and cash flow statement for the nine month period ending 30 September 2006
- In section 28.6 financial reports for Air Iceland
  - In section 28.6.1 audited 2003 – 2005 annual reports
  - In section 28.6.2 interim income statement, balance sheet and cash flow statement for the nine month period ending 30 september 2005
  - In section 28.6.3 audited interim income statement, balance sheet and cash flow statement for the nine month period ending 30 September 2006
- In section 28.7 financial reports for Bluebird Cargo
  - In section 28.7.1 audited 2003 – 2005 annual reports
  - In section 28.7.2 interim income statement, balance sheet and cash flow statement for the nine month period ending 30 September 2005
  - In section 28.7.3 audited interim income statement, balance sheet and cash flow statement for the nine month period ending 30 September 2006
- In section 28.8 Icelandair Group's interim statements for 2006
  - In section 28.8.1 compiled interim account for the period ending 31 March 2006
  - In section 28.8.2 reviewed interim account for the period ending 30 June 2006
  - In section 28.8.3 audited interim account for the period ending 30 September 2006
- In section 28.9 Icelandair Group's pro-forma statements
  - In section 28.9.1 pro forma statement of earnings for the year 2005
  - In section 28.9.2 pro forma opening balance sheet 1 January 2006

SHARE CAPITAL

The Company was founded on 20 December 2005, under the name Icelandair Group ehf., with a total share capital of ISK 500,000 nominal value. At a shareholders meeting held on 17 February 2006 it was decided to increase the share capital of the Company by ISK 3,500,000 nominal value. After that increment the share capital of the Company was ISK 4,000,000 nominal value. At a shareholders meeting held on 30 May 2006 it was decided to increase the share capital by ISK 2,996,000,000 nominal value. After that increment the share capital of the Company was ISK 3,000,000,000 nominal value. At a shareholders' meeting held on 15 November 2006 it was decided to decrease the share capital by ISK 2,000,000,000 nominal value. Accordingly, the share capital of the Company is ISK 1,000,000,000 nominal value and is divided into equal numbers of shares each having a nominal value of ISK 1.0. All the shares have been fully paid.

At the same shareholders´ meeting the Company was altered from being private limited company to public limited company, in accordance to article 107 of Act no. 138/1994 respecting Private Limited Companies. The name of the Company was changed also, to Icelandair Group hf.

Neither the Company nor its subsidiaries hold any shares in the Company.

On 24 October 2006, Icelandair Group Holding issued convertible bonds in the nominal amount of ISK 2,000,000,000. All rights and obligations attached to the bonds have now been taken over by Icelandair Group.

If there will be no dividends paid in the next five years and no share increase, except to meet the requirements of the convertible bonds, then, given that the owners of the bonds will use all their rights to convert bonds to shares, the total number of shares in the Company, at the maturity of the bond, will be 1,067,340,067 and the owners of the bonds will therefore hold 67,340,067 of those shares.

Glitnir banki hf. is the owner of all these convertible bonds described.

ARTICLES OF ASSOCIATION

OBJECT AND PURPOSE

The object of the Company, according to Article 3 of its Articles of Association, is investment in equity holdings, particularly holdings in other companies engaged in air carrier operations, tourist services and transport operations, buying and selling real estate, credit operations and other related operations.

BOARD OF DIRECTORS AND MANAGEMENT

The Company's board of directors shall consist of seven members and two alternate members, elected at the Annual General Meeting for a term of one year. Those who intend to stand for election to the board of directors shall inform the Board in writing of their intention at least five days before the Annual General Meeting, or Extraordinary Shareholders' Meeting at which elections are to take place. Only those who have informed the Board of their candidacy are eligible.

The Company's board of directors is the supreme authority in the Company's affairs between shareholders' meetings and shall ensure that the organisation and activities of the Company's operation are generally in correct and good order. The board of directors shall appoint a CEO for the Company and decide the terms of his or hers employment. The board of directors and the CEO are responsible for the management of the Company. The company's board of directors shall ensure that there is adequate supervision of the company's accounts and the disposal of its assets and shall adopt working procedures in compliance with the Companies Act. Only the board of directors may assign powers of procuration. The signatures of the majority of the members of the Board shall bind the Company.

The board of directors elects a chairman and vice chairman from among its members, and otherwise allocates its obligations among its members as needed. The chairman calls board meetings. A meeting shall also be held if requested by a member of the board of directors or the CEO. Meetings of the board are valid if attended by a majority of the members of the board. However, important decisions shall not be taken unless all members of the Board have had the chance to discuss the matter, if possible. The outcome of issues shall be decided by force of vote and in the event of an equality of votes the issue shall be regarded as rejected. The CEO attends meetings of the board of directors, even though he or she is not a member of the Board, and has the right to debate and submit proposals unless otherwise decided by the Board in individual cases. A book of minutes shall be kept of proceedings at meetings and shall be signed by participants in the meeting. A board member, or the CEO, who is not in agreement with a decision by the board of directors is entitled to have his or her dissenting opinion entered in the book of minutes.

The CEO has charge of the day-to-day operations of the company and shall observe the policy and instructions set out by the company's board of directors. Day-to-day operations do not include measures which are unusual or extraordinary Such arrangements can only be made by the CEO in accordance with special authority from the Board, unless it is impossible to await the decision of the Board without seriously disadvantaging the operation of the Company. In such instances, the CEO shall consult with the chairman, if possible, after which the board of directors shall immediately be notified of the measures. The CEO shall ensure that the accounts and finances of the Company conform to the law and accepted practices and that the disposal of the property of the Company is secure. The CEO shall provide the Members of the board of directors and Company auditors with any information pertaining to the operation of the Company which they may request, as required by law.

RIGHTS, PREFERENCES AND RESTRICTIONS OF SHARES

All voting shares carry equal rights and no privileges are attached to shares in the Company. All the shares are freely transferable, unless otherwise provided for by law.

ACTIONS NECESSARY TO CHANGE SHAREHOLDERS' RIGHTS

According to Article 23 of the Articles of Association the Articles of Association may only be amended at a lawful Annual General Meeting or extraordinary shareholders' meeting, provided that the notice of the meeting clearly indicates that such an amendment is proposed and outlines the main substance of the amendment. A decision is valid only if it has the support of at least 2/3 of the cast votes and the support of shareholders controlling at least 2/3 of the share capital represented at the meeting, provided always that no other force of vote is required by these Articles or statutory law, cf. Article 93 of the Companies Act.

SHAREHOLDERS' MEETINGS

Shareholders exercise their powers at shareholders' meetings, which hold the company's supreme powers, within the limits provided for in the Articles of Association and law. All shareholders are permitted to attend shareholders' meetings, address them and exercise their voting rights. The auditor of the Company and the CEO shall have full rights to address and submit motions at shareholders' meetings even if they are not shareholders. A shareholder may appoint a proxy to attend meetings on his/her behalf, in which case the proxy shall submit a written and dated letter of proxy. Also, shareholders may attend the meeting together with an advisor; the advisor, however, does not have the right to address the meeting, to submit motions or to vote. The board of directors may invite experts to attend individual meetings, if their opinion or assistance is required.

Shareholders' meetings shall be called at the discretion of the board of directors, at the request of the Company auditor , or if shareholders controlling 1/10 of the shares of the Company request a meeting by a written notice. The request shall include a statement to the board of directors explaining the reason for the request, and the board of directors shall notify shareholders of the business on the agenda in the notice of the meeting. When a lawful request for a meeting has been submitted, the board of directors shall call a meeting no later than fourteen days from the time that the request was received. If the board of directors has not called a meeting within that time, shareholders may require a meeting to be called pursuant to the provisions of the Companies Act.

Shareholders' meetings, including the Annual General Meeting, shall be called by a notice to each shareholder by registered mail, telegram or by other verifiable means or, at the discretion of the board of directors, by a notice in the newspapers, with at least one week's notice. A shareholders' meeting is valid, regardless of attendance, if the meeting has been properly convened. Attendance shall be determined based on the number of ballots delivered.

The notice of a shareholders' meeting shall specify the business to be addressed at the meeting. If the agenda includes motions to amend the Articles of the Company, the substance of the motion shall be included in the notice of the meeting. Seven days before a shareholders' meeting, at the latest, an agenda, final submissions and, in the case of annual general meetings, the annual accounts, report of the board of directors and the auditor's report shall be laid open for inspection by shareholders at the Company office.

Each shareholder shall be entitled to have a specific item of business included on the agenda of a shareholders' meeting, provided that such shareholder submits a written request to this effect to the board of directors of the Company with sufficient advance notice for the item to be included on the agenda in accordance with these Articles.

Items of business which are not included on the agenda may not be accepted for final decision at a shareholders' meeting except with the consent of all the shareholders in the Company, but a resolution may be passed to provide guidance to the board of directors of the Company. Lawfully submitted motions for amendments may be put to a vote at the meeting itself, even if they have not been laid open for inspection by shareholders. An Annual General Meeting is always permitted to conclude matters which it is required to address pursuant to statutory law or the Company Articles.

The Annual General Meeting shall be held before the end of May.

II.
SECURITIES NOTE

SUMMARY

SECURITIES NOTE

REGISTRATION DOCUMENT

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1 RISK FACTORS

Investors are reminded that investing in shares entails risk, as the decision to invest is based on expectations and not promises. Investors must rely primarily on their own judgement regarding any decision to invest in a company's shares, bearing in mind the business environment in which the company operates, anticipated profits, external conditions and the risk inherent in the investment itself. Prospective investors are advised to contact experts such as licensed financial institutions to assist them in their assessment of the shares in the company as an investment option. Investors are advised to consider their legal status, including taxation issues that may concern the purchase or sale of shares in the company and seek external and independent advice in that respect.

Prior to making any investment decision regarding shares in the Company, please consider all the information in this document, the Registration Document of the Prospectus and in particular, the risks and uncertainties described below. The risks and uncertainties described below are some of those that may materially affect a company and any investment made in its shares. If any combination of these events occurs, the trading price of the shares could decline and investors might lose part of their investment or even all of it. Additional risks and uncertainties that do not currently exist, that are not presently considered material, or of which the company is unaware may also impair the business and operations of the company. These risks and uncertainties could have a material adverse impact on the business, income, profits, assets, liquidity and share price of the company.

1.1 RISKS INHERENT IN EQUITY INVESTMENTS

Equity investments involve a variety of risks. Examples of such risk factors that may have a material effect on the price of a company's shares, and thereby on the investment value, are market risk, liquidity risk and counterparty risk. The share price can fluctuate considerably due to factors such as variations in operating income or cost, changes in the market environment, adverse commentary about the company and its operations and services in the media and changes to the company's competitive position. Moreover, it must be kept in mind that shares are a subordinated claim on the assets of companies. This means that in the event of the company's liquidation, the shareholders will receive what is left after all other claims have been met. In many countries, shares have yielded a better return than bonds measured over long periods of time. Nevertheless, long periods can also be found where the return on shares has been worse than on bonds and even negative. Those who intend to invest in the Company should know that there is no guarantee of a return on their investment in the future and investors should bear in mind that even though stocks can provide a good return in general, there is always a risk that an investment in the shares of individual companies will decline in value. It is therefore suggested that those who intend to invest in shares pay close attention to diversifying their risk and seek investment advice.

Due to the fact that the Company's shares will be traded on the ICEX Main List, those investing in them will thereby become subject to public regulation relating to securities transactions, such as rules relating to takeover bids, public disclosure of ownership stakes, etc.

1.2 FURTHER SHARE CAPITAL INCREASE CAN DILUTE SHAREHOLDINGS

If new shares in the Company are issued, the proportional shareholding of those who already hold shares in the Company will be reduced accordingly, unless they themselves acquire the new shares pro rata to their existing holdings. The purpose of increasing capital is normally to finance projects with the long-term intention of making the Company more valuable in the future. Shareholders may therefore be faced with increased risk to their investment alongside the dilution of their shares. It is possible that the Company will consider increasing its share capital further in the future in order to finance its continuing growth.

1.3 SHAREHOLDER STRUCTURE

The structure of shareholder ownership can be a risk factor for investors. A lack of leading investors or large concentrations of ownership are examples of circumstances that can have negative effects on the operations of the Company. Investors should be aware of the fact that ownership of the Company can change rapidly and without any prior warning.

2 PERSONS RESPONSIBLE

2.1 THE ISSUER

The Issuer, Icelandair Group hf, Icelandic ID-No. 631205-1780, registered office at Reykjavík Airport, 101 Reykjavík, the Chairman of the Board of Directors and the CEO, whose names appear below, accept responsibility for the information contained in this Prospectus. Having taken all reasonable care to ensure that such is the case, they hereby declare that the information contained in the Prospectus is, to the best of their knowledge, in accordance with the facts and contains no omission likely to affect its import.

Reykjavík, 9 February 2007.
On behalf of the board of directors and Icelandair Group hf.
Reykjavik Airport, 101 Reykjavik, Iceland

Finnur Ingólfsson
Chairman of the board of directors
Icelandic ID No. 080854-3829

Jón Karl Ólafsson
CEO
Icelandic ID No. 120958-2759

2.2 LISTING ADVISOR

Glitnir banki hf., Icelandic ID-No. 550500-3530, Kirkjusandur 2, 155 Reykjavík, Iceland, has been advisor to the Company on the listing of the shares and the preparation of this Securities Note.

Glitnir banki hf., in its capacity as Listing Advisor declares that in preparing this Prospectus it has gathered the data which, in its estimation, are necessary to provide a true and fair view of the Company and The Shares. Glitnir banki hf., hereby declares that, having taken all reasonable care to ensure that such is the case, the information contained in this Prospectus is, to the best of its knowledge, in accordance with the facts and contains no omission likely to affect its import.

Reykjavík, 9 February
On behalf of Glitnir banki hf.
Kirkjusandur 2, 155 Reykjavík, Iceland

Einar Örn Ólafsson
Executive Director of Corporate Finance
Icelandic ID No. 230273-2949

3 NOTICE TO INVESTORS

This Securities Note and any document forming a part of the Prospectus published on 12 February 2007, is not being distributed in, and must not be mailed or otherwise distributed or sent in or into any country in which distribution would require any additional registration measures or other measures to be taken, other than as applicable under Icelandic law and regulations, or would be in conflict with any law or regulation in such country.

The Company's total issued share capital amounts to 1,000,000,000 shares, each with a nominal value of ISK 1.0. The Company has applied for listing on the ICEX Main List. The Company does fulfil the conditions for listing on the ICEX Main List, including conditions regarding share distribution, size and number of shareholders. The Company, in its current form, has not been in operation for three years as required by ICEX. However although the Company was founded, as a holding company,20 December 2005 its subsidiaries all have operation histories longer than the three year requirement. Therefore the board of directors of ICEX granted the company an exeption from that condition provided the Company was able to provide sufficient financial information as considered by ICEX.

This Securities Note concerns the listing of the Shares on the ICEX Main List.

The admission to trading will proceed pursuant to Icelandic law and regulations. Directive 2003/71/EC of the European Parliament and of the Council of 4 November 2003 has been implemented into Icelandic Law. The ICEX has, in its authority under agreement between it and the Icelandic Financial Supervisory Authority regarding the review and approval of prospectuses, reviewed and approved this Securities Note, which is published in English only.

In the event of any significant new factor, material mistake or inaccuracy relating to information included in this Securities Note which is capable of affecting the assessment of the Shares the company, the Company will issue an announcement that will be published on the ICEX news page.

This Securities Note should by no means be viewed or construed as a promise by the Company, Glitnir banki hf. (the Listing Advisor) or other parties of future success either in operations or return on investments. Investors are reminded that investing in shares entails risk, as the decision to invest is based on expectations and not promises. Investors must rely primarily on their own judgement regarding any decision to invest in the Company's shares, bearing in mind inter alia the business environment in which the Company operates anticipated profits, external conditions and the risk inherent in the investment itself. Prospective investors are advised to contact experts, such as licensed financial institutions, to assist them in their assessment of the shares in the Company as an investment option. Investors are advised to consider their legal status, including taxation issues that may concern the purchase or sale of shares in the Company and seek external and independent advice in that respect.

Not withstanding a special statement to the contrary references to any Acts or regulations are references to Acts passed by the Icelandic parliament and regulations issued by Icelandic governmental agencies unless otherwise clear from the context.

The registered auditor of Icelandair Group hf. is KPMG hf., Icelandic ID No. 590975-0449, Borgartún 27, IS-105 Reykjavík, Iceland.

4 REFERENCES AND GLOSSARY OF ABBREVIATIONS

References to “Icelandair Group”, “the Group” and “the Company” in this Securities Note shall be construed as referring to Icelandair Group hf., Icelandic ID No. 631205-1780 and its subsidiaries, unless otherwise clear from the context. Icelandair Group hf. is the legal Icelandic name of the Company.

References to “Icelandair Group Holding” in this Securities Note shall be construed as referring to Icelandair Group Holding hf., Icelandic ID No. 591006-2150 unless otherwise clear from the context. Icelandair Group Holding hf. was merged with Icelandair Group hf. effective as of 1 November 2006 as agreed by a shareholders meeting of Icelandair Group Holding on 29 December 2006.

References to “the Shares” in this Securities Note shall be construed as referring to the 1,000,000,000 shares in Icelandair Group hf. and which this Securities Note covers, unless otherwise clear from the context.

References to “the Prospectus” in this Securities Note shall be construed as referring to the Company’s prospectus dated 9 February 2007, consisting of this Securities Note, a Registration Document and a Summary.

References to “ICEX” in this Securities Note shall be construed as referring to the Iceland Stock Exchange, i.e. to Kauphöll Íslands hf., Icelandic ID No. 681298-2829, unless otherwise clear from the context. References to the “ICEX Main List” in this Securities Note shall be construed as referring to the Main List at the Iceland Stock Exchange, unless otherwise clear from the context.

References to “the ISD” in this Securities Note shall be construed as referring to Icelandic Securities Depository, i.e. to Verðbréfaskráning Íslands hf., Icelandic ID No. 500797-3209, unless otherwise clear from the context.

References to “Listing Advisor” in this Securities Note shall be construed as referring to Glitnir banki hf., Icelandic ID No. 550500-3530, unless otherwise clear from the context.

References to “the Merger” in this Securities Note shall be construed as referring to the merger of Icelandair Group and Icelandair Group Holding, effective as of 1 November 2006 as agreed on shareholders meetings of Icelandair Group on 28 December 2006 and Icelandair Group Holding on 29 December 2006.

Abbreviations used in this Securities Note

CEO	Chief Executive Officer
PAYE	Pay-As-You-Earn
The Companies Act	Act No. 2/1995 on Public Limited Companies
The Securities Act	Act No. 33/2003 on Securities Transactions

5 KEY INFORMATION

5.1 WORKING CAPITAL

It is the Company's opinion that the working capital is sufficient for its present requirements. The Company has on average negative working capital requirement since the international flight operations receive advance payments but pay costs after the service has been provided.

5.2 CAPITALIZATION AND INDEBTEDNESS

The following table shows the consolidated capitalization and indebtedness of Icelandair Group as of 31 October 2006 taking into account the Merger and increased indebtedness of Icelandair Group Holding following the purchase of Icelandair Group on 15 October 2006. The balance sheet was generated internally and has not been audited.

Table 1. The consolidated capitalization and indebtedness of the Company

Current liabilities			
Guaranteed	0		
Secured	12,506		
Unguaranteed/Unsecured	18,013	Cash and cash equivalents	4,490
Total current liabilities	30,519		
Non-current liabilities		Current financial receivables	6,345
Guaranteed	0		
Secured	11,200	Current bank debt	(3,600)
Unguaranteed/unsecured	7,614	Current portion of non current debt	(12,200)
Total non-current liabilities	18,814	Trade and other payables	(11,319)
		Other current finacial debt	(3,400)
Shareholders' equity		Current financial debt	(30,519)
Share capital	1,000		
Share premium	25,223	Non-current bank loans	(17,814)
Other reserve	834	Other non-current loans	(1,000)
Total equity	27,057	Non-current financial indebtedness	(18,814)
Total capitalisation	76,390	**Net financial indebtedness**	(38,498)

5.3 INTEREST OF NATURAL AND LEGAL PERSONS INVOLVED

Glitnir banki hf., Icelandic ID No. 550500-3530, reg. office Kirkjusandur 2, 155 Reykjavík, Iceland. Glitnir banki hf. directly holds 45,416,707 shares in the Company.

Glitnir banki hf. holds 47.5% of the share capital in Fjárfestingafélagið Máttur ehf., which holds 111,111,111 shares in Icelandair Group hf.

Glitnir banki hf. directly holds 30.1% of the share capital in Naust ehf. which holds 148,148,148 shares in Icelandair Group hf. Glitnir banki hf. also holds 12% of the share capital in BNT hf., which holds 49.9% of the share capital in Naust ehf. Furthermore, Glitnir banki hf. holds 47.5% of the share capital in Fjárfestingafélagið Máttur ehf. which in turn has 12% ownership in BNT hf.

All figures are as of 7 February 2007. For the companies mentioned above, voting rights are held by the majority of each company directly owning shares in Icelandair Group.

Einar Sveinsson, a member of the Board of Directors of the Company is also a member of the Board of Directors of Glitnir banki hf.

The Company does not hold any shares in Glitnir banki hf. and Glitnir banki hf. is not the main commercial bank used by the Company.

There is no other material interest of natural and legal persons involved.

6 INFORMATION CONCERNING THE SECURITIES

6.1 TOTAL SHARE CAPITAL

The total number of issued shares in the Company is 1,000,000,000 all of same class. All shares in the Company are issued in ISK.

6.2 TYPE AND CLASS OF SHARES

The Company's share capital consists of one class of shares, each share having a nominal value of ISK 1.0. The ISIN number of the shares is IS0000013464. The shares' ticker symbol in the trading system of the ICEX will be ICEAIR, the symbol used for Icelandair Group Holding from the time of listing on 14 December 2006.

6.3 LEGISLATION

The Company is registered in Iceland and operates pursuant to the Companies Act. All shares in the Company have been issued under the Companies Act.

6.4 FORM

The Company's shares are all issued electronically at the ISD, which is located at Laugavegur 182, 105 Reykjavik, Iceland. All shares are registered under the name and Icelandic ID Number of the relevant shareholders or their nominees.

The electronic registration of securities is governed by the Act on Electronic Registration of Titles to Securities, No. 131/1997 and Regulation No. 397/2000, which is issued in accordance with that Act. A printout from the ISD on the ownership of shares in the Company is considered a valid proof of registration of the shares. Registry of title in a securities depository constitutes full proof of title to shares in the Company and adequate basis for entry in the register of shares. Dividends and announcements shall at any given time be sent to the party registered in the Company's share register as owner of the shares in question. The Company shall be in no way liable if payments or announcements do not reach their recipients because a change of address has not been notified.

6.5 SHARE RIGHTS

All the shares of the Company carry equal rights. The Company's shares carry no special rights and no restrictions are placed on them. A party acquiring a share in the Company cannot exercise its right as a shareholder unless its name has been registered in the share registry or it has announced and proven its ownership of the share.

Owners of the Company's share capital have the right to vote at shareholders' meetings, the right to receive dividends when declared, enjoy pre-emptive rights to new shares, unless waived, and the right to a share in any surplus in case of liquidation, all according to share ownership, statutes and the Company's Articles of Association in effect at any given time.

A resolution on the distribution of dividends shall be made at an annual general meeting, which shall be held before the end of May each year. A shareholder who owns shares on the date when the dividend payment falls due is entitled to the dividend. This right to a dividend lapses four years later according to the Act No. 14/1905 on the Expiry of Debts and Other Claim Rights. The Company and its subsidiaries are subject to legal restrictions on the amount of dividends that can be paid to shareholders according to the Companies Act. There are no special restrictions or procedures regarding dividend payment for non-resident shareholders. The Company has no formal dividend policy although the Company's board of directors has the intention to set a policy of paying 35-50% of each year's earnings before interest and taxes in dividends to shareholders.

Rights to electronic shares must be registered at the ISD if they are to enjoy legal protection against legal executions and disposal by means of an agreement. It is forbidden to issue share certificates for registered rights according to an electronic share or endorse them, and such transactions are void. Registration of the ownership of an electronic share at the ISD, subsequent to a Securities Depository final entry, formally gives a registered owner legal authorization to the rights for which he is registered. Priority of incompatible rights is determined by the chronological order of requests from the Banks' Data Central reaching the Securities Depository. No redemption provisions, conversion provisions or special restrictions regarding dividends have been attached to the securities.

6.6 SHARE CAPITAL DECREASE – CONVERTIBLE BONDS – AUTHORIZATION

The Company was founded on 20 December 2005, under the name Icelandair Group ehf., with a total share capital of ISK 500,000 nominal value. At a shareholders meeting held on 17 February 2006 it was decided to increase the share capital of the Company by ISK 3,500,000 nominal value. After that increment the share capital of the Company was ISK 4,000,000 nominal value.

At a shareholders meeting held on 30 May 2006 it was decided to increase the share capital by ISK 2,996,000,000 nominal value. After that increment the share capital of the Company was ISK 3,000,000,000 nominal value. At a shareholders' meeting held on 15 November 2006 it was decided to decrease the share capital by ISK 2,000,000,000 nominal value. Accordingly, the share capital of the Company is ISK 1,000,000,000 nominal value and is divided into equal numbers of shares each having a nominal value of ISK 1.0. All the shares have been fully paid.

At the same shareholders´ meeting the Company was altered from being a private limited company to a public limited company, in accordance to article 107 of Act no. 138/1994 on Private Limited Companies.

Icelandair Group Holding hf. issued on the 24 October 2006, bonds in the nominal amount of ISK 2,000,000,000 that give the owner the right to convert the principal of the claim under the bonds to shares at the base rate of 29.7 which will be as amended in accordance with dividend payments and share capital increase as described in the articles of association of Icelandair Group Holding hf. With the Merger, the obligations under the bonds where taken over by the Company and provisions added to the Articles of Association of the Company to evidence this.

If there will be no dividends paid in the next five years and no share increase, except to meet the requirements of the convertable bonds, then, given that the owners of the bonds will use all their rights to convert bonds to shares, the total number of shares in the Company, at the maturity of the bond, will be 1,067,340,067 and the owners of the bonds will therefore hold 67,340,067 of those shares.

Glitnir banki hf. is the owner of all the convertible bonds described in this subsection.

The Board of Directors of the Company is authorised to approve a stock option plan for key employees of the Company and/or its subsidiaries, which entails their permission to buy further specified shares in the Company. For the purpose of fulfilling the said stock option plan, the Board of Directors of the Company is authorised to increase the company's share capital by up to ISK 60,000,000 – sixty million Icelandic krónur – in nominal value, or up to 6% of the listed shares of the company at any time, which shall be used in fulfilment of the said stock option contracts. The selling price of shares in the Company to holders of stock options shall be decided by the Board of Directors of the Company at any time; the price shall not be lower than 27 times nominal, but shall in other respects be determined by the average rate of market trading in the company's share ten days prior to the signature of each stock option contract. This authorisation to increase the company's share capital is effective for five years from its approval and may be exercised by the Board in part or in full, at the discretion of the Board. Shareholders' pre-emptive rights pursuant to the Company's Articles of Association do not apply to the increase in share capital pursuant to the above authorisation to the Board of Directors. In the event that the share capital of the Company is increased during the period of the authorisation beyond ISK 1,000,000,000, the authorisation shall be increased so as to remain always at the level of 6% of the total share capital of the Company at any time. The shares in question are not subject to trading restrictions. The new shares shall carry rights in the company from the date of their listing.

6.7 TRANSFERABILITY OF THE SHARES

There are no limitations on the transferability of the Company's shares, and shareholders may pledge their shares unless prohibited from doing so by law. Only general legislative rules apply to the transfer of shares in the Company. Nevertheless, it should be noted that individual shareholders may have agreed that their shares are subject to certain restrictions.

Langflug ehf., Naust ehf. and Urður ehf. have all made lock-up agreements with the Listing Advisor. Both Langflug ehf. and Urður ehf. have a lock-up on all their shares until 14 December 2007. Naust ehf. has lock-up on 1/2 of its shares until 14 December 2007, and lock-up on ¼ on its shares until 14 June 2007 but other parts of the shares are not subject to lock-up. The total number of shares subject to lock-up until 14 December 2007 is 449,629,630 and the total number of shares subject to lock up until 14 June 2007 is 37,037,037. This totals 486,666,667 shares or 48.7% of the total share capital. Information about the companies subject to lock-up on their shares is provided in the following subsections.

6.7.1 LANGFLUG EHF.

Langflug ehf. Icelandic ID No. 660906-1500, reg. office Suðurlandsbraut 18, 108 Reykjavík, Iceland is an investment company owned 75% by Eignarhaldsfélagið Samvinnutryggingar svf., Icelandic ID No. 550269-0589, reg. office Kringlan 7, 103 Reykjavík, Iceland and 25% by Finnur Ingólfsson, the Chairman of the Board of Directors of the Company, Icelandic ID No. 080854-3829.

6.7.2 NAUST EHF.

Naust ehf., Icelandic ID No. 460906-0320, reg. office Suðurlandsbraut 18, 108 Reykjavík, Iceland is an investment company. The company is jointly owned by the following parties:

- BNT hf. Icelandic ID No. 530206-0250, reg. office Suðurlandsbraut 18, 108 Reykjavík, Iceland, owns 49.9% of the share capital in Naust ehf.
- Glitnir banki hf., Icelandic ID No.550500-3530, reg. office Krikjusandur, 155 Reykjavík, Iceland, owns 30.1% of the share capital in Naust ehf.
- Hrómundur ehf., Icelandic ID No. 491188-2519, reg. office Bakkaflöt 10, 210 Garðabæ, Iceland, owns 10.0% of the share capital in Naust ehf. Hrómundur ehf. is owned by Einar Sveinsson.
- Hafsilfur ehf., Icelandic ID No. 610469-0199, reg. office Lindarflöt 51, 210 Garðabæ, Iceland, owns 10.0% of the share capital in Naust ehf. Hafsilfur ehf. is owned by Benedikt Sveinsson.

6.7.3 URÐUR EHF.

Urður ehf., Icelandic ID No., 681290-1689, reg. office Austurstræti 5, 155 Reykjavík, Iceland, is owned 66.7% by Blue Sky Transport Holding S.A. a company owned 100% by Ómar Benediktsson, Icelandic ID No.221059-4689 and 33.3% by FSP hf. Icelandic ID No. 510400-2670, Skógarhlíð 12, 105 Reykjavík, Iceland.

6.8 MANDATORY TAKEOVER BIDS AND/OR SQUEEZE-OUT AND SELLOUT RULES

Mandatory bid

The Company will be subject to Section VI of the Securities Transactions Act, No. 33/2003, with subsequent amendments, which implemented Directive 2004/25/EC of the European Parliament and of the Council of 21 April 2004 on takeover bids (the Takeover Directive). Under the Securities Transactions Act, if a party, directly of indirectly, acquires control of the Company, it is obliged to make an offer, within four weeks, to the other shareholders to acquire their shares at a price not less than the highest price paid for the shares by the acquirer or its concert parties during the previous six months. ‘Control’ means that the party and any party acting in concert with it has acquired (i) in total at least 40% of the voting rights in the Company, (ii) under an agreement with other shareholders, the right to control at least 40% of the voting rights in the Company, (iii) the right to appoint or dismiss the majority of the board of directors of the Company.

No party, directly of indirectly, owns a controlling stake in the Company.

Squeeze-out / sell-out

Under The Securities Act, if the acquirer, or any of its concert parties, acquires more than 90% of the shares or voting rights of the Company, the acquirer and the board of directors of the Company may decide to redeem the remaining shares. Notice of such decision, including the terms of the redemption, registered mail, telegram or by other verifiable means or, at the discretion of the Board of Directors, by a notice in the newspapers, with at least one week's notice. If the acquirer demands the redemption within three months from the end of the takeover period, the price offered in the takeover bid shall be considered a fair redemption price, unless the acquirer, or any of its concert parties, has paid a higher price during the takeover period or during the three months following on from the end of the takeover period. In the notice of the decision, shareholders shall be encouraged to transfer their shares to the acquirer within four weeks. If they do not transfer their shares within four weeks, the redemption price shall be deposited in an account in their name, on which the acquirer shall becomes the rightful owner of the shares and the share certificates of former shareholders shall become void.

Should the acquirer, or any of its concert parties, acquire more than 90% of the shares or voting rights of the Company, any one of the minority shareholders shall be able to demand that the acquirer redeem his shares. If the minority shareholder demands redemption within three months of the end of the takeover period, the price offered in the takeover bid shall be considered a fair redemption price, unless the acquirer, or any of its concert parties, has paid a higher price during the takeover period or during the three months following on from the end of the takeover period. More detailed provisions on redemption, including the appointment of valuators if no agreement is reached on the redemption price, can be found in the Companies Act.

6.9 PUBLIC TAKEOVER BIDS BY THIRD PARTIES

The Company's shares have not before been listed or admitted to trading on ICEX or any other regulated marked. Accordingly, the Company's shares have not been subject to rules on public takeover bids. However, Icelandair Group is a former subsidiary of Icelandair Group Holding, which was listed on ICEX Main List on 14 December 2006. AS discussed in detail in section 8, the two companies have now been merged.

6.10 TAX ISSUES

The following is a summary of certain Icelandic tax consequences for shareholders. The summary does not cover tax issues in cases where securities are held as assets in business operations or by a partnership. The tax treatment for holders depends in part on their particular circumstances. Each shareholder should consult a tax advisor regarding the tax consequences which may arise for such person as a result of buying or selling our Shares, including the applicability and effect of foreign income tax regulations and provisions contained in treaties to avoid double taxation. Foreign parties should obtain information on a possible double taxation treaty with the country of residence. If such a treaty has been made, the party should establish which country has the right to tax.

6.10.1 TAX CONSIDERATIONS FOR RESIDENTS OF ICELAND

Individuals

Capital gains from sale of shares are taxable in Iceland pursuant to current laws. For individuals, capital income such as interest, dividends (see "-Taxation of Dividends") and capital gains are taxed as income from capital. The tax rate is 10%. Upon sale of shares, the shareholder's average acquisition costs for all shares of the same class and type will be used as the tax base on which the capital gain of the sale is calculated. Individuals can use losses from sale of shares in limited liability companies within the same calendar year and offset them against capital gains from sale of shares. Losses from sale of shares can not be carried forward and offset against future capital gains from sale of shares.

Taxable Legal Entities

For taxable legal entities, all gains from sale of shares will be taxed as income from business activities at a rate of 18% in the case of a limited liability company.

Gains on shares are taxable in full regardless of how long the company has owned the shares. A gain is calculated as the difference between the sale price and average cost price of all shares of the same class and type.

Taxable legal entities may postpone the payment of the tax of capital gains from the sale of shares for a period of up to two years starting at the end of the year when the shares are sold. In the case of shares in limited liability companies (domestic or foreign) acquired within the same period, the tax base of those shares is reduced by the capital gains, which in turn will not be taxed until the sale of such shares. When shares are sold the taxable amount is the sale price less the tax base used to buy the shares. If taxable legal entities do not invest the proceeds of the sale of shares in limited liability companies within the required timeframe, the capital gains are taxed on the second year from the sale.

Capital losses from sale of shares within the same tax year may be offset only against the capital gains on shares. Losses from sales of shares cannot be carried forward as losses from regular activities.

Specific tax consequences may be applicable to certain categories of companies, such as mutual funds and investment companies.

Taxation of Dividends

The Company is obligated to withhold 10% tax on paid out dividends in the case of individuals and resident companies. Companies may have a deduction of the same amount as the dividends received and consequently there is no effective tax burden for companies. The 10% withheld by the Company is in accordance with the Company's legal responsibilities under law respecting withholding taxes. If the withholding tax is higher than levied tax, then the difference will be refunded upon assessment of tax returns.

6.10.2 TAX CONSIDERATIONS FOR NON-RESIDENTS OF ICELAND

The Company is obligated to withhold 10% tax on dividends paid to individuals not residents of Iceland (absent treaty provisions to the contrary). The Company is obligated to withhold 15% tax on dividends paid to foreign legal entities unless there is a tax treaty in place lowering the percentage. Qualified companies may apply for a reimbursement and/or an advance relief under relevant provisions in double taxation treaties.

Gains from the sale of shares in Icelandic companies by residents of non treaty countries are subject to taxation in Iceland. The tax rate is 10% for individuals and 15% for legal entities.

Icelandic brokers as well as Icelandic persons acting as intermediaries are technically required to withhold the tax from the sale price unless they have been furnished with the Director of Internal Revenue's confirmation of the seller's exemption from such taxation prior to the transaction. Residents of treaty countries can apply for formal confirmation of their exemption from such taxation from the Director of Internal Revenue.

6.10.3 STAMP DUTY

The Company's shares are subject to stamp duty in Iceland, which the Company shall pay within two months of the issue of the shares. Stamp duty has been paid on all issued shares. Transfer of shares is not subject to stamp duty.

7 ADMISSION TO TRADING

7.1 LISTING ON ICEX

The Board of Directors was authorised by the shareholder's meeting on 28 December 2006 to merge the Company with Icelandair Group Holding and list the Company on the ICEX Main List. The objectives of the listing are to increase liquidity of the shares, reach a broader range of investors and to get better price information on the shares.

The Board of ICEX has agreed to the listing of the Company's entire issued shares on the ICEX Main List. The Company currently fulfils ICEX condition for listing, including conditions regarding size, share distribution and number of shareholders.

7.2 ADMISSION TO TRADING

The earliest date on which the Shares will to be admitted to trading on ICEX Main List is 12 February 2006.

7.3 REGULATED MARKETS

The Board of ICEX has agreed on admission to trading of the Shares on the ICEX Main List. The Company's board of directors has not made any resolution on seeking an admission to trading for the Company's shares on other regulated markets than the ICEX.

7.4 MARKET MAKING

According to two separate agreements, Glitnir banki hf. and Straumur Burðarás Investment Bank hf. will act as market makers for the Company's shares after the listing on ICEX Main List.

Glitnir banki hf. shall through its own account submit daily bids and asks to the ICEX for a minimum of ISK 15 million (purchasing price) on each side at a price determined by the market maker on any given occasion. The maximum bid/ask spread may not exceed 1.0% and the difference from the last price paid may not exceed 3.0%. The market maker is obliged to provide liquidity for up to ISK 150 million per day.

Straumur Burðarás Investment Bank hf. shall through its own account submit daily bids and asks to the ICEX for a minimum of ISK 13.5 million (purchasing price) each side at a price determined by the market maker on any given occasion. The maximum bid/ask spread may not exceed 1.0% and the difference from the last price paid may not exceed 3.0%. Straumur Burðarás Investment Bank is obliged to provide liquidity for up to ISK 150 million per day.

8 THE MERGER

In October 2006, Icelandair Group Holding was formed with the sole purpose of purchasing all shares in Icelandair Group and at the same time acquiring all the shares in Icelandair Group hf.'s subsidiaries. On 14 December 2006, following the acquisition, Icelandair Group Holding was listed on the ICEX Main List.

In the process leading up to the public offer and a listing on the Iceland Stock Exchange of Icelandair Group Holding, the board of Directors and the Management of Icelandair Group Holding and Icelandair Group came to the conclusion that it would best serve the company and its shareholders if the two companies, Icelandair Group Holding and Icelandair Group were to be merged effective as of 1 November 2006. By doing this, the annual statements of 2006, for Icelandair Group Holding, the then presumably listed company, will best reflect its operational results. With the two companies merged before year end 2006, the statements will reflect the operations for the whole of 2006. This gives investors, creditors and all those who have made significant agreements with Icelandair Group or any of its subsidiaries a better view of the operational results. This is especially important with regards to existing leasing contracts and communications with creditors.

On 29 December, 2006 the shareholders of Icelandair Group Holding hf. agreed to the merger of Icelandair Group Holding hf. and Icelandair Group hf. effective as of 1 November 2006. Since Icelandair Group has made various contracts and guarantees on behalf of its subsidiaries in its normal course of business, while Icelandair Group Holding has not, as it was only established on 15 October 2006, the companies will be merged under the name of Icelandair Group hf., Icelandic ID No. 631205-1780.

On the merger of Icelandair Group Holding hf. and Icelandair Group hf. the former company will be liquidated and its shareholders will receive shares in Icelandair Group hf. in the nominal value of ISK 1,000,000,000 as payment for their shares in Icelandair Group Holding hf. As there are also 1,000,000,000 shares in Icelandair Group hf. shareholders will receive one share in Icelandair Group hf. for every share they hold in Icelandair Group hf. before the merger. KPMG hf. acting as advisor on the merger did not find any complications in relations to the proposed merger and concluded that the compensation for the shares in Icelandair Group Holding hf. is fair and reasoned.

As a result of this merger Icelandair Group Holding hf. will be delisted after the close of trading the trading day before the listing of Icelandair Group hf.

9 COST OF THE ADMISSION TO TRADING

The total cost of the admission to trading of this share capital on the Main List of the ICEX is estimated at ISK 10 million, including charges from ICEX. All costs of the admission to trading will fall on the Company.

10 ADDITIONAL INFORMATION

The Listing Advisor has been advisor to the Company on the listing of the shares and the preparation of the Prospectus.

III.
REGISTRATION DOCUMENT

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1 RISK FACTORS

Investing in shares is subject to numerous risks. Prior to making any investment decision regarding shares in the Company, please consider all the information in this document and, in particular, the risks and uncertainties described below. The risks and uncertainties described below may materially affect the Company and any investment made in its shares. If any combination of these events occurs, the trading price of the shares could decline and investors might lose part or even all of their investment. Additional risks and uncertainties that do not currently exist, that are not presently considered material, or of which the Company is unaware, may also impair the business and operations of the Company. These risks and uncertainties could have a material adverse impact on the business, income, profits, assets, liquidity and share price of the Company.

1.1 GENERAL RISKS ASSOCIATED WITH INVESTMENTS IN EQUITIES

Experience shows that equities are generally a more profitable investment than bonds in the long term. Yield on equities consists of dividend payments, on the one hand, and of the change in share prices on the other, profit or loss resulting from the difference between the price per share on purchase and at sale.

It must be borne in mind that, all other things being equal, investing in equities involves greater risk than investing in bonds. Equity prices generally undergo greater fluctuations than do bond values. The risk involved in investing in individual companies can be spread by investing in a portfolio of companies of different types. Nevertheless, it is not possible to avoid risks that affect the equity market as a whole, e.g. currency exchange fluctuations, changes in general interest rates, risks accompanying political developments, changes in the economic outlook, etc.

1.2 RISKS RELATING TO THE AIRLINE INDUSTRY

The Company owns and operates companies in the airline, transportation and tourism industries.

1.2.1 COMPETITION

The level of competition amongst airlines is high and pricing decisions are heavily dependent on competition from other airlines. The low marginal costs relating to servicing additional customers on scheduled flights, compared to flying with vacant seats, has also resulted in the airline industry being susceptible to fare discounting. On-line sales have increased the price transparency in the air travel market, which has in turn resulted in more intense competition. The Company is also to some extent subject to competition from alternative ways of travelling, such as buses and private cars. Should competition increase even further in any of the Company's key markets, including the Icelandic market, this might have a considerable effect on the Company's profitability.

1.2.2 FUEL PRICE AND AVAILABILITY

As an airline operator, the Company is highly sensitive to jet fuel prices and availability. Jet fuel has been, and is expected in the future to be, subject to significant price volatility and fluctuations in supply and demand. Increased costs and/or restricted availability of aviation fuel may affect the profitability of the Company. In order to control better the Company’s risks relating to volatile fuel prices, the Company has a policy of hedging a portion of its projected aviation fuel requirements. However, hedging is also subject to risks. If fuel prices continue to rise, this will damage the Company's cost structure and its competitiveness vis-à-vis its competitors which have greater hedging. If prices were to fall at the same time as the Company has a higher level of hedging than its competitors, this would damage its competitiveness. Recently, when high fuel prices have prevailed, airlines have been more efficient in passing price increases on to their customers through fuel surcharges and other methods. If fuel prices continue to rise, there is no guarantee that the increase in cost can be passed on to customers due to the competitive nature of the airline industry, and therefore the Company could be affected adversely. If fuel prices remain high for an extended period, long-haul flights will become proportionally more expensive to operate, and therefore leisure travellers may prefer travelling shorter distances due to the lower cost involved.

1.2.3 SEASONALITY

The Company operates in a seasonal industry where there has traditionally been higher demand for air travel in the summer. This seasonal pattern explains why the Company operates more aircraft during the summer season than during other seasons and has relatively better results in the second and third quarters of the year than in the first and fourth. Lower demand for air travel, flight cancellations or other factors affecting aircraft utilization would therefore have a proportionately greater impact on the Company during the summer than during other periods.

1.2.4 REGULATIONS

Air transportation is subject to intensive regulations. An Air Operator's Certificate (AOC) has been issued to the relevant subsidiaries[1] of Icelandair Group authorising it to conduct its airline operations. There is no guarantee that the Company will be issued such licenses in the future. Occasionally the FAA (Federal Aviation Administration, a US government agency responsible for overseeing air transportation in the USA) and its European counterparts issue directives and other regulations relating to the maintenance of aircraft that result in significant costs for the Company. There is no guarantee that the Company will be compensated for this through higher ticket prices, and so it is likely that the Company will be adversely affected. The Company's operating authority is subject to aviation agreements between governmental authorities of the European Union and the respective countries. Those agreements are periodically subject to renegotiation. Changes in the aviation policies of those countries could result in the termination of such agreements and adversely affect the Company's operations. Individual airline regulators, including the one in Iceland, may impose restrictions and requirements that would impact the Company's profitability.

1.2.5 "OPEN SKIES" AGREEMENT

The United States and Europe have been conducting negotiations regarding an "open skies" agreement between the two markets. The agreement would bring together the world's two largest aviation markets, allowing EU and US airlines to fly to any destination and charge prices at their own discretion. If the agreement materializes, competition on transatlantic flights is likely to increase, which could adversely affect the profitability of business of the Company, which is competing on transatlantic markets. These negotiations are still in progress, however, and their outcome is difficult to predict.

1.2.6 AIRPORT ACCESS

At some airports, an air carrier needs landing and takeoff authorisations (slots) before being able to introduce new services or expand existing ones. The Company is dependent on its slots in order to be able to compete. If the Company is not able to secure and retain slots, this could limit its ability to compete in certain markets. Generally, access to airports is furthermore vital to minimize the likelihood of delays, which can be detrimental to the Company's profitability.

1.2.7 ECONOMICAL EFFECTS

Generally, the airline industry tends to experience greater profitability during times of economic prosperity. Consequently, the Company is dependent on the state of the economy in the countries in which it operates. In a depressed economy, consumers are likely to reduce air travel, which could affect both load factors and yield. Even though the Company has worked extensively on reducing its fixed costs to reduce the adverse effects of reduced demand, it will most likely be negatively affected in the case of a depressed economy.

1.2.8 STRIKES

The airline industry is an inherently labour-intensive industry. The majority of the Company's employees are unionized, and are represented by several unions, each of which has its own contract on salaries and benefits with the Company. Each contract comes up for renegotiation every few years, and every time this happens there is a risk

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[1] Icelandair, Bluebird Cargo, Air Iceland and LatCharter (owned by Loftleiðir-Icelandic) have been issued an AOC.

that the parties will not reach an agreement; such situations may end in a strike. Strikes can affect the Company heavily and in the worst case halt the operation of one or more of its subsidiaries. Strikes in the aviation industry can be extremely expensive for airlines due to the nature of the business, which is burdened with high fixed costs. Additionally, the Company could be adversely affected by strikes of airport employees or any other employee group that it depends on but does not constitute part of its own staff. In addition to relying on hired personnel, the Company relies on third parties to provide its customers with services on behalf of and in cooperation with it. Any inability of the relevant third parties to provide such services may impact the business.

1.2.9 TERRORIST INCIDENTS AND EPIDEMICS

Following the terrorist attacks of 11 September 2001, demand for airline travel dropped. Similarly, many airlines were affected by the outbreak of SARS (Severe Acute Respiratory Syndrome) in 2003. The occurrence of another large scale terrorist attack or an outbreak of a disease that resulted in fear of travelling could depress the aviation industry and affect the Company adversely.

1.2.10 AIRPORT SECURITY

Security measures have in the past disrupted airline business on temporary or long-term grounds and have the potential to do so in the future. For instance, a terrorism alert in the United Kingdom in August this year led to additional security restrictions at UK airports and delays and cancellation of certain flights. Such increased security measures may affect the Company’s profitability.

1.2.11 ACCIDENTS

Icelandair Group, like all airline operators, could be affected adversely if one of its aircraft were to be involved in an accident or crash. This may involve not only the repair or replacement of damaged or lost aircraft and the consequent temporary or permanent loss from services, but also claims from injured passengers and the surviving relatives of deceased passengers. Even though the Company is insured, the insurance cover may be inadequate, in which case it might face significant losses. Additionally, if an aircraft from the Company is involved in an accident, this might create a public perception that the Company's aircraft are not reliable, which in turn could harm the business.

1.3 OTHER OPERATIONAL RISKS

1.3.1 AIRCRAFT PRICING AND AVILABILITY

Aircraft prices and leasing are cyclical by nature. If the value of a type of aircraft drops due to lower demand for air travel or any other reason, the value of those craft and their leasing rates will be affected. If this happens, the Company's profitability could be adversely affected. On the other hand, when the Company needs to replace the aircraft which it is currently operating, add new aircraft or renegotiate leasing agreements, the Company’s aircraft operating cost could increase or decrease depending on the market conditions at that time, which would affect its profitability. The Company owns a number of aircraft, the value of which will have to be tested for impairment when there is an indicator of impairment. Such impairment tests could result in the writing down of the aircraft if the market value and the value in use are below the carrying value of the aircraft.

The Company owns approximately 50% of its aircraft operating in scheduled flights (see section 13 for details) while the other are leased with various time span for flexibility, should the Company need to react to lower demand.

The Company mainly uses Boeing aircraft, since the Company’s management believes that they satisfactorily meet its objectives of minimizing costs while maximizing passengers' security. Generally, having only one aircraft supplier makes the Company dependent on the supplier to a certain extent.

1.3.2 INTERNATIONAL OPERATIONS

Operating in foreign markets exposes the Company to various risks. There is a risk that its prospects in some markets could diminish due to various factors, including political changes, exchange controls and taxation.

1.3.3 KEY EMPLOYEES

The Company is dependent on its key employees and their willingness to continue working for it. There is, however, no guarantee that it will be able to retain all of them in the future. If the Company loses any of them, it could be adversely affected. Should members of key personnel decide to join competitors or start competing independently with the Company, this may have consequences for the Company's business.

In order to reduce the risk of losing key employees, the company aims to offer competitive salary packages to its key employees. This includes linking the management's salary to results of individual subsidiaries. Furthermore, the Company actively manages its information systems to keep know-how within the company. Employment agreements with certain key employees also contain provisions that exclude them from working for competitors for up to 24 months after their resignation. Both these factors should reduce the consequences for the company if one of its key employees decides to resign.

1.3.4 COMPUTER AND COMMUNICATION SYSTEMS

An increasing proportion of ticket sales take place over the internet. The Company's planning, communication and revenue management systems are also computer based. These systems are vulnerable to disruptions that are beyond the Company's control. Possible disruptions could result from viruses, hackers, equipment failure, power failure, natural disasters and human errors. The Company has various initiatives in place to minimize the risk of failure to those systems but there can be no assurance that these initiatives will adequately prevent disruption to its systems.

1.3.5 INSURANCES

The Company carries insurance for passenger liability, property damage, public liability and all-risk cover for damaged aircraft. There may be losses which the business may suffer that are not covered by insurance. Furthermore, individual losses may exceed the cover under applicable insurance. In both cases, losses may subject the Company to considerable financial harm.

1.3.6 ANTI-TRUST REGULATIONS

Due to the favourable market position of some of Icelandair Group's subsidiaries in Iceland, Icelandair Group is subject to even more stringent anti-trust regulations than a company with a smaller market share would be. This places some limitation on the Company's ability to grow in the Icelandic market. Furthermore, the Company is from time to time involved in disputes with its competitors over alleged breaches of anti-trust regulations. Should the competition authorities reach the conclusion that the Company has breached such regulations, this may have serious consequences for the Company which may include substantial fines and affect its ability to conduct its business in the usual manner. Current legal and arbitration proceedings are detailed in section 25.

1.4 FINANCIAL RISK

1.4.1 EXCHANGE-RATE AND INTEREST-RATE RISKS

Fluctuations in exchange rates and interest rates, and exchange-rate risk posed by trading between Group companies with different functional currencies, can materially impact the Company's profitability. The Company aims to reduce as much as possible of any such risk by actively managing its currency balance and interest-rate risk.

1.4.2 LIQUIDITY RISK

The Company could, in the future, face the risk of having insufficient working capital to meet its requirements, e.g. due to inability or difficulties in liquidating its assets. This risk is mitigated to some extent by maintaining liquid assets. Liquidity risk is also reduced to some extent by the nature of the Company's business, as it realises income before paying the cost associated with providing the services.

1.5 REGULATORY AND LEGAL RISK

1.5.1 APPLICABLE LAW

The Company and its subsidiaries are subject to various laws and regulations. Changes to the Group's applicable laws, or it becoming subject to different laws, might have an impact on how it continues to conduct its business.

1.5.2 COVENANTS – CONTRACTUAL RISK

The Company is contractually bound to honour various contracts in leasing and financing agreements. Should the Company become unable to fulfil the relevant covenants, or for some reason discontinue to do so, the lessors and financiers may become entitled to rescind these agreements, which might have financial consequences for the Company.

1.5.3 SECURITIES REGULATION

Since the Company's shares will be traded on the Iceland Stock Exchange, it will be subject to Icelandic securities regulations, e.g. those in the Securities Act, government regulations and rules adopted by the Iceland Stock Exchange. When the Company will be listed on Iceland Stock Exchange it will endeavour to comply with the said provisions, and any violation of these provisions may have a financial impact on it. Serious breaches may result in the Iceland Stock Exchange ceasing to list the Company's securities. Should the Company violate the relevant rules, this may furthermore impact its reputation and consequently result in the price of its shares dropping.

1.5.4 REGULATIONS

The airline operations and other aspects of the Company's business, such as the segments relating to tourism, are subject to the condition that various regulations and public permits have been issued. If any regulations were changed, or permits cancelled or not renewed, this might affect the Company adversely.

1.5.5 LITIGATION

Given the Company's size and the scope of its operations, it tends to be involved in some form of litigation at any given time. Currently the Company is involved in various legal disputes, including cases before the Competition authorities. Current legal and arbitration proceedings are detailed in section 25.

1.5.6 TRADEMARKS AND INTELLECTUAL PROPERTY

The Company owns a number of trademarks and other intellectual property through its operational subsidiaries. It has used all means available to secure legal rights to such trademarks and intellectual property. Should it, for some reason, be unable to continue to rely on the relevant intellectual property rights, this could impact its business.

1.5.7 INTERNAL CONTROLS

The Company is dependent on having sufficient internal controls in place in various areas, including controls relating to the handling of electronic documents. The Company has focused on strengthening such controls. Should such controls prove, however, to be insufficient, this may have a negative impact on the Company.

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1.5.8 TAX

The Company could be affected by changes in tax legislation in any country that affects its financial results. Icelandair Group is not aware of any current tax inspection concerning the Group which may have a material impact on its shares, and has no reason to believe that any such inspection is imminent. Investigation of the Company's tax filings, as for any other company, may be initiated at a later stage in accordance with relevant regulations and affect its prospects.

There could be some tax risks regarding withholding tax. In the Company's senior management opinion there is uncertainty regarding its duty to withhold tax on lease payments of aircraft leased from foreign lessors from countries that don't have a tax treaty with Iceland. In practice the Company has never done so. Management has taken steps to clarify the situation and they believe that they are using the same approach as has been used in the past by Icelandic companies but the risk is that tax authorities would conclude that the Company's approach to withholding tax issues do not fully comply with tax legislation applicable in this context.

The Listing Advisor has not independently verified these issues and recommends that any potential investor investigate this issue in general. No assurance can be given on the likelihood of payments having to be made in this respect, or on the possible scale of such payments. When FL Group sold its shares in the Company they agreed to compensate Icelandair Group hf. fully for any payments above ISK 500 million which might be paid by the Company or subsidiaries because of tax obligations prior to the sale and thereby limiting the Company's risk to ISK 500 million.

Currently there are no tax disputes in progress between the Company and tax authorities.

2 PERSONS RESPONSIBLE

2.1 THE ISSUER

The Issuer, Icelandair Group hf., Icelandic ID-No. 631205-1780, registered office at Reykjavík Airport, 101 Reykjavík, the chairman of the board of directors and the CEO, whose names appear below, accept responsibility for the information contained in this Registration Document. Having taken all reasonable care to ensure that such is the case, they hereby declare that the information contained in the Registration Document is, to the best of their knowledge, in accordance with the facts and contains no omission likely to affect its import.

Reykjavík, 9 February 2007.
On behalf of the board of directors and Icelandair Group hf.
Reykjavik Airport, 101 Reykjavik, Iceland

Finnur Ingólfsson
Chairman of the board of directors
Icelandic ID No. 080854-3829

Jón Karl Ólafsson
CEO
Icelandic ID No. 120958-2759

2.2 THE LISTING ADVISOR

Glitnir banki hf., Icelandic ID-No. 550500-3530, Kirkjusandur 2, 155 Reykjavík, Iceland, is the Listing Advisor and has been advisor to the Company on the listing of the shares and the preparation of this Registration Document.

Glitnir banki hf., in its capacity as the Listing Advisor declares that in preparing this Prospectus it has gathered the data which, in its estimation, are necessary to provide a true and fair view of the Company and the Shares. Glitnir banki hf., hereby declare that, having taken all reasonable care to ensure that such is the case, the information contained in this Registration Document is, to the best of its knowledge, in accordance with the facts and contains no omission likely to affect its import.

Reykjavík, 9 February 2007.
On behalf of Glitnir banki hf.
Kirkjusandur 2, 155 Reykjavík, Iceland

Einar Örn Ólafsson
Executive Director of Corporate Finance
Icelandic ID No. 230273-2949

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2.3 STATUTORY AUDITORS

The registered auditor of Icelandair Group hf. is KPMG hf., Icelandic ID No. 590975-0449, Borgartún 27, IS-105 Reykjavík, Iceland. KPMG hf. has reviewed the consolidated pro forma income statement for 2005 for Icelandair Group, interim report for Icelandair Group for the first six months of 2006 and the opening pro forma balance sheet at 1 January 2006 for Icelandair Group. KPMG hf. has furthermore audited the interim report of Icelandair Group hf. dated 30 September 2006 and the annual accounts of Icelandair, Icelandair Cargo, Loftleiðir Icelandic and Air Iceland for the years ended December 31, 2003, 2004 and 2005. KPMG has also audited the income statements, balance sheets and statements of cash flow for the first nine months of 2006 for Icelandair, Icelandair Cargo, Loftleiðir-Icelandic, Bluebird Cargo and Air Iceland. In addition to this KPMG has compiled the interim consolidated balance sheet of Icelandair Group hf. and its subsidiaries as of 31 March 2006 and the related consolidated income statement and statement of cash flows for the three months then ended.

KPMG confirms that all information in this Registration Document regarding financial information is consistent with the said financial statements.

Reykjavik, 9 February 2007.
On behalf of KPMG hf.

Jón Sigurdur Helgason
State authorised public accountant
Icelandic ID No. 050269-3619

Sæmundur Valdimarsson,
State authorised public accountant
Icelandic ID No. 070263-4409

Grant Thornton endurskoðun ehf., Icelandic ID No. 430190-1999, Suðurlandsbraut 20, 108 Reykjavík, Iceland, has audited the financial information for Bluebird Cargo ehf. for the years ending December 31, 2003, 2004 and 2005. Grant Thornton confirms that all information in this Registration Document regarding financial information for Bluebird Cargo is consistent with the said financial statements it has audited.

Reykjavik, 9 February 2007.
On behalf of Grant Thornton endurskoðun ehf.,

Theódór S. Sigurbergsson
State authorised public accountant
Icelandic ID No. 060459-3049

3 DOCUMENTS ON DISPLAY

For the life of this Registration Document, published on 12 February 2007, the following documents may be inspected on Icelandair Group hf.'s registered office Reykjavik Airport, 101 Reykjavik, Iceland and on Icelandair Group hf.'s website http://www.icelandairgroup.is:

- The Registration Document, Security Note and Summary dated 9 February 2007.
- Icelandair Group hf.'s Articles of Association.
- Stock Option Plan for Key Employees of Icelandair Group hf. dated 29 December 2006.
- The consolidated balance sheet for Icelandair Group hf. dated 31 October 2006. The balance sheet is internally generated and has not been audited.
- Icelandair Group hf.'s reviewed consolidated pro forma income statements for the financial year ending 31 December 2005 (including the auditors' reports issued in respect thereof).
- Icelandair Group hf.'s reviewed consolidated pro forma opening balance sheet at 1 January 2006 (including the auditors' reports issued in respect thereof).
- Icelandair Group hf.'s interim report for the first three months of 2006, reviewed interim report for the six months ending 30 June 2006 and audited interim report for the nine months ending 30 September 2006.
- The audited annual financial statements for Icelandair, Icelandair Cargo, Loftleiðir-Icelandic, Bluebird Cargo and Air Iceland for each of the financial years ending 31 December 2003, 31 December 2004 and 31 December 2005 (including the audit reports issued in respect thereof).
- The audited interim income statements, balance sheets and cash flow statements for Icelandair, Icelandair Cargo, Loftleiðir-Icelandic, Bluebird Cargo and Air Iceland for the first nine months of 2006.
- The interim financial statement for Icelandair, Icelandair Cargo, Loftleiðir Icelandic, Bluebird Cargo and Air Iceland for the first nine months of 2005. These accounts have not been audited.
- The Merger plan for Icelandair Group Holding hf. and Icelandair Group hf. dated 15 November 2006.
- Assessors report on the merger of Icelandair Group Holding hf. and Icelandair Group hf.

4 DOCUMENTS INCORPORATED BY REFERENCE

For the life of the Registration Document, published on 12 February 2007, the following documents in the Registration Document for Icelandair Group Holding dated 26 November 2006 shall be deemed to be incorporated in, and to form part of this Registration Document. The non-incorporated parts of the Registration Document for Icelandair Group Holding are either not relevant for the investor or covered elsewhere in this Prospectus. Icelandair Group Holding has been merged with Icelandair Group and all information relevant to the merged company are contained in this Prospectus.

- In section 28.1 merger plan for Icelandair Group Golding hf. and Icelandair Group hf. and KPMG report on the merger of Icelandair Group Holding hf. and Icelandair Group hf.
- In section 28.3 financial reports for Icelandair ehf.
- In section 28.3.1 audited 2003 – 2005 annual reports
    - In section 28.3.2 interim income statement, balance sheet and cash flow statement for the nine month period ending 30 September 2005
    - In section 28.3.3 audited interim income statement, balance sheet and cash flow statement for the nine month period ending 30 September 2006
- In section 28.4 financial reports for Flugleiðir frakt ehf. (Icelandair Cargo)
    - In section 28.4.1 audited 2003 – 2005 annual reports
    - In section 28.4.2 interim income statement, balance sheet and cash flow statement for the nine month period ending 30 September 2005
    - In section 28.4.3 audited interim income statement, balance sheet and cash flow statement for the nine month period ending 30 September 2006
- In section 28.5 financial reports for Loftleiðir-Icelandic ehf.
    - In section 28.5.1 audited 2003 – 2005 annual reports
    - In section 28.5.2 interim income statement, balance sheet and cash flow statement for the nine month period ending 30 September 2005
    - In section 28.5.3 audited interim income statement, balance sheet and cash flow statement for the nine month period ending 30 September 2006
- In section 28.6 financial reports for Air Iceland
    - In section 28.6.1 audited 2003 – 2005 annual reports
    - In section 28.6.2 interim income statement, balance sheet and cash flow statement for the nine month period ending 30 september 2005
    - In section 28.6.3 audited interim income statement, balance sheet and cash flow statement for the nine month period ending 30 September 2006
- In section 28.7 financial reports for Bluebird Cargo
    - In section 28.7.1 audited 2003 – 2005 annual reports
    - In section 28.7.2 interim income statement, balance sheet and cash flow statement for the nine month period ending 30 September 2005
    - In section 28.7.3 audited interim income statement, balance sheet and cash flow statement for the nine month period ending 30 September 2006
- In section 28.8 Icelandair Group's interim statements for 2006
    - In section 28.8.1 compiled interim account for the period ending 31 March 2006
    - In section 28.8.2 reviewed interim account for the period ending 30 June 2006
    - In section 28.8.3 audited interim account for the period ending 30 September 2006
- In section 28.9 Icelandair Group's pro-forma statements
    - In section 28.9.1 pro forma statement of earnings for the year 2005
    - In section 28.9.2 pro forma opening balance sheet 1 January 2006

5 REFERENCES

References to "Icelandair Group", "the Group" and "the Company" in this Registration Document shall be construed as referring to Icelandair Group hf., Icelandic ID No. 631205-1780 and its subsidiaries, unless otherwise clear from the context.

References to "Icelandair Group Holding" in this Registration Document shall be construed as referring to Icelandair Group Holding hf., Icelandic ID No. 591006-2150, unless otherwise clear from the context. Icelandair Group Holding hf. was merged with Icelandair Group hf. effective 1 November 2006.

References to "Icelandair Group's employees" shall be constructed as referring to employees of Icelandair Group and its subsidiaries.

References to "FL Group" in this Registration Document shall be construed as referring to FL GROUP hf., Icelandic ID No. 601273-0129 and its subsidiaries, unless otherwise clear from the context. When referred to FL Group it applies to the company after the annual meeting in 2005 when the name of the company was changed to FL GROUP hf.

References to "Flugleiðir" in this Registration Document shall be construed as referring to FL GROUP hf., Icelandic ID No. 601273-0129 and its subsidiaries, unless otherwise clear from the context. When referred to Flugleiðir it applies to the company before the annual meeting in 2005 when the name of the company was changed to FL GROUP hf.

References to "the Shares" in this Registration Document shall be construed as referring to the 1,000,000,000 issued shares in Icelandair Group hf., unless otherwise clear from the context.

References to Icelandair Group's subsidiaries are by their English brand names as defined in Table 7.

References to "ICEX" in this Registration Document shall be construed as referring to the Iceland Stock Exchange, i.e. to Kauphöll Íslands hf., Icelandic ID No. 681298-2829, unless otherwise clear from the context. References to the "ICEX Main List" in this Registration Document shall be construed as referring to the Main List at the Iceland Stock Exchange, unless otherwise clear from the context.

References to "the ISD" in this Registration Document shall be construed as referring to Icelandic Securities Depository, i.e. to Verðbréfaskráning Íslands hf., Icelandic ID No. 500797-3209, unless otherwise clear from the context.

References to "the Listing Advisor" and "Glitnir" in this Registration Document shall be construed as referring to Glitnir banki hf., Icelandic ID No. 550500-3530, unless otherwise clear from the context.

References to "the Merger" in this Registration Document shall be construed as referring to the merger of Icelandair Group and Icelandair Group Holding, effective as of 1 November 2006, as agreed on shareholders meetings of Icelandair Group hf. on 28 December 2006 and Icelandair Group Holding hf. on 29 December 2006. The two companies merged under the name and ID of Icelandair Group hf. Icelandic ID No. 631205-1780.

In section 26, Articles of Association, references to Managing Director shall be construed as referring to the Chief Executive Officer (CEO) of Icelandair Group hf,

6 THIRD PARTY INFORMATION

Where third party information has been used in this Registration Document, the source of such information has been identified. As far as the Company is aware and able to ascertain from information published by those third parties, no facts have been omitted which would render the reproduced information inaccurate or misleading.

Three third party sources are used in relations to market information, those are Icelandic Tourist Board, Icelandic Civil Aviation Administration and The Boeing Company.

With respect to the merger plan of Icelandair Group Holding and Icelandair Group, at the request of Icelandair Group Holding's board of directors, a report was prepared by KPMG Endurskoðun hf. Icelandic ID No. 590975-0449, Borgartún 27, IS-105 Reykjavík, Iceland. This report is included in the Appendix as part of the merger plan. KPMG is also the Company's auditor.

7 NOTICE TO INVESTORS

This Registration Document and any document forming a part of the Prospectus published on 12 February 2007, is not being distributed in, and must not be mailed or otherwise distributed or sent in or into any country in which distribution would require any additional registration measures or other measures to be taken, other than as applicable under Icelandic law and regulations, or would be in conflict with any law or regulation in such country.

The Company's total issued share capital amounts to 1,000,000,000 shares, each with a nominal value of ISK 1.0. The Company has applied for listing on the ICEX Main List. The Company does fulfil the conditions for listing on the ICEX Main List regarding share distribution, size and number of shareholders. The Company, in its current form, has not been in operation for three years as required by ICEX. However, its subsidiaries all have operation histories longer than the three year requirement. Therefore the board of directors of ICEX granted the company an exemption from that condition.

This Registration Document concerns the listing of the Shares on the ICEX Main List.

The admission to trading will proceed pursuant to Icelandic law and regulations. Directive 2003/71/EC of the European Parliament and of the Council of 4 November 2003 has been implemented into Icelandic Law. The ICEX has, in its authority under agreement between it and the Icelandic Financial Supervisory Authority regarding the review and approval of prospectuses, reviewed and approved this Registration Document, which is published in English only.

This Registration Document has been prepared to provide clear and thorough information on the consolidated company Icelandair Group hf. Investors are encouraged to acquaint themselves thoroughly with this Registration Document. They are advised to pay particular attention to the chapter Risk Factors. Investors should note that the Company was founded in December 2005. Financial audited information for Icelandair Group only exists for the first nine months of 2006. However, financial information for Icelandair Group's largest subsidiaries (Icelandair, Icelandair Cargo, Loftleiðir-Icelandic, Bluebird Cargo and Air Iceland) undertaking for last three years are included in this Registration Document as well as accounts for the first nine months of 2005 and 2006. These subsidiaries represented approximately 88% of the Company's revenue on 30 September 2006 and therefore represent the operations of Icelandair Group. The Company believes that these statements give clear and thorough historical financial information for investors.

In the event of any significant new factor, material mistake or inaccuracy relating to information included in this Registration Document which is capable of affecting the assessment of the Shares the company, the Company will issue an announcement that will be published on the ICEX news page.

This Registration Document should by no means be viewed or construed as a promise by the Company, Glitnir banki hf. (the Listing Advisor) or other parties of future success either in operations or return on investments. Investors are reminded that investing in shares entails risk, as the decision to invest is based on expectations and not promises. Investors must rely primarily on their own judgement regarding any decision to invest in the Company's shares, bearing in mind inter alia the business environment in which the Company operates anticipated profits, external conditions and the risk inherent in the investment itself. Prospective investors are advised to contact experts, such as licensed financial institutions, to assist them in their assessment of the shares in the Company as an investment option. Investors are advised to consider their legal status, including taxation issues that may concern the purchase or sale of shares in the Company and seek external and independent advice in that respect.

Not withstanding a special statement to the contrary references to any Acts or regulations are references to Acts passed by the Icelandic parliament and regulations issued by Icelandic governmental agencies unless otherwise clear from the context.

8 SELECTED FINANCIAL INFORMATION

Detailed information concerning the Company's financial position is presented in sections 20 to 24. Information on the five largest subsidiaries of Icelandair Group is presented in section 21, containing each company's income statement and statement of cash flow for the years 2003-2005 and the first nine months of 2005 and 2006 and each company's balance sheet for the years 2003-2005 and the first nine months of 2006. Information on the Group's performance for the first 9 months of 2006 is given in section 22, while discussion on pro forma statement of earnings for the year 2005 is provided in section 23 and the consolidated balance sheet for Icelandair Group hf. is provided in section 24. The balance sheet is internally generated and the pro forma accounts are provided for illustrative purposes only. This section provides selected information from the sections mentioned above.

8.1 ANNUAL ACCOUNTS OF SELECTED SUBSIDIARIES

Table 1. Key Figures for Icelandair for the period 2003-2005 and the first nine months of 2005 and 2006. Balance Sheet figures are for the end of each period. All figures in ISK million.

	2003	2004	2005	1/1-30/9 2005	1/1-30/9 2006
Profit and loss account					
Transport revenue	18.161	20.409	23.818	18.805	22.408
Aircraft and air crew lease	4.991	6.968	6.161	4.450	5.682
Other operating revenue	2.548	1.680	1.484	1.069	1.437
Operating expenses before depreciation	(24.900)	(27.981)	(30.483)	(22.975)	(26.406)
Depreciation	(125)	(691)	(684)	(528)	(949)
EBITDA	800	1.076	980	1.349	3.121
EBIT	675	385	296	821	2.172
Pre-tax profit	613	127	557	825	2.677
Income tax	(111)	(28)	(108)	(155)	(488)
Profit for the period	502	99	449	670	2.189
Balance Sheet					
Total assets	9.502	9.339	11.662		29.009
Liabilities	6.226	6.219	8.020		23.076
Equity capital	3.276	3.120	3.642		5.933
Cash flow					
From operating activities	3.831	1.464	2.781	3.502	5.082

Table 2. Key Figures for Icelandair Cargo for the period 2003-2005 and the first nine months of 2005 and 2006. Balance Sheet figures are for the end of each period. All figures in ISK million.

	2003	2004	2005	1/1-30/9 2005	1/1-30/9 2006
Profit and loss account					
Cargo and mail	2.698	3.207	3.053	2.203	2.923
Aircraft lease	436	442	282	166	710
Service revenue	759	1.096	1.213	876	1.126
Other operating revenue	23	27	34	20	40
Operating expenses before depreciation	(3.723)	(4.449)	(4.550)	(3.218)	(4.654)
Depreciation	(12)	(21)	(26)	(19)	(14)
EBITDA	193	323	32	46	145
EBIT	181	302	6	27	131
Pre-tax profit	219	301	9	25	146
Income tax	(1)	(55)	(2)	(5)	(28)
Profit for the period	218	246	7	20	118
Balance Sheet					
Total assets	877	958	1.014		1.237
Liabilities	762	604	882		989
Equity capital	115	354	133		248
Cash flow					
From operating activities	411	162	18	98	(2)

Table 3. Key Figures for Loftleiðir-Icelandic for the period 2003-2005 and the first nine months of 2005 and 2006. Balance Sheet figures are for the end of each period. All figures in ISK million.

	2003	2004	2005	1/1-30/9 2005	1/1-30/9 2006
Profit and loss account					
Aircraft and air crew lease	3.902	5.454	5.573	4.161	4.947
Sale of assets	0	0	0	0	411
Other operating revenue	14	19	36	25	29
Operating expenses before depreciation	(4.160)	(5.365)	(5.248)	(3.895)	(5.093)
Depreciation	(2)	(5)	(4)	(3)	(15)
EBITDA	(244)	108	361	291	294
EBIT	(246)	103	357	288	280
Pre-tax profit	(231)	85	325	261	334
Income tax	73	(15)	(60)	(49)	(40)
Profit for the period	(158)	70	265	212	294
Balance Sheet					
Total assets	424	554	1.172		2.671
Liabilities	752	775	1.095		2.351
Equity capital	(328)	(221)	77		320
Cash flow					
From operating activities	58	292	522	429	31

Table 4. Key Figures for Bluebird Cargo for the period 2003-2005 and the first nine months of 2005 and 2006. Balance Sheet figures are for the end of each period. All figures in ISK million.

	2003	2004	2005	1/1-30/9 2005	1/1-30/9 2006
Profit and loss account					
Sales income	1.489	2.136	2.241	1.702	2.164
Other operating income	5	74	21	18	15
Operating expenses before depreciation	(920)	(1.500)	(1.766)	(1.359)	(1.632)
Depreciation	(251)	(269)	(223)	(186)	(193)
EBITDA	575	711	496	360	547
EBIT	324	441	273	175	354
Pre-tax profit	150	296	158	85	276
Income tax	(5)	(47)	(35)	(21)	(50)
Profit for the period	145	249	123	64	226
Balance Sheet					
Total assets	2.655	2.429	2.409		2.914
Liabilities	2.188	1.778	1.615		1.804
Equity capital	467	651	794		1.109
Cash flow					
From operating activities	407	468	438	295	570

Table 5. Key Figures for Air Iceland for the period 2003-2005 and the first nine months of 2005 and 2006. Balance Sheet figures are for the end of each period. All figures in ISK million.

	2003	2004	2005	1/1-30/9 2005	1/1-30/9 2006
Profit and loss account					
Transport revenue	1.972	2.259	2.591	1.885	2.355
Cargo and mail	105	97	103	76	111
Aircraft and air crew lease	408	520	498	415	413
Other operating revenue	438	465	358	337	327
Operating expenses before depreciation	(2.527)	(2.723)	(3.068)	(2.328)	(2.555)
Depreciation	(132)	(193)	(182)	(137)	(183)
EBITDA	397	618	483	384	650
EBIT	265	425	302	248	467
Pre-tax profit	227	384	247	214	403
Income tax	158	(70)	(46)	(39)	(74)
Profit for the period	385	314	201	175	329
Balance Sheet					
Total assets	1.552	1.813	1.218		3.576
Liabilities	687	978	537		2.565
Equity capital	866	835	681		1.011
Cash flow					
From operating activities	286	877	282	136	238

8.2 2006 INTERIM REPORT

Table 6. Key figures for Icelandair Group the first three quarters of 2006 and combined for the first nine months of 2006. All figures in ISK million.

	Q1 2006 1/1-31/3	Q2 2006 1/4-30/6	Q3 2006 1/7-30/9	2006 1/1-30/9
Profit and loss account				
Transport revenue	5.555	9.613	12.480	27.648
Aircraft and air crew lease	2.217	2.268	3.290	7.775
Other operating revenue	1.823	2.600	3.707	8.130
Operating expenses before depreciation	(9.860)	(12.917)	(15.056)	(37.833)
Depreciation	(827)	(409)	(642)	(1.878)
EBITDAR	304	2.385	5.432	8.121
EBITDA	(265)	1.564	4.421	5.720
EBIT	(1.092)	1.155	3.779	3.842
Pre-tax profit	(677)	1.560	3.056	3.939
Income tax	122	(281)	(515)	(674)
Profit for the period	(555)	1.279	2.541	3.265
Balance Sheet				
Total assets				67.892
Liabilities				44.510
Equity capital				23.382
Cash flow				
From operating activities	979	3.857	1.557	6.393

9 INFORMATION ABOUT THE COMPANY

9.1 HISTORY AND DEVELOPMENT

The history of Icelandair Group's predecessors dates back to 1937, almost as long as the history of commercial aviation in Iceland, which began in 1919, less than 16 years after the Wright brothers made the first ever powered flight. Icelandair Group predecessor, Flugleiðir hf., was established in Reykjavik on July 20, 1973, by a merger of Flugfélag Íslands hf. and Loftleiðir hf. Flugleiðir's main operations during the period 1937-2005 were in aviation. Flugleiðir was listed on the ICEX Main List in 1992.

At Flugleiðir's annual general meeting in 2005, the company's name was changed to FL Group and in October 2005, fundamental changes took place by which investment activities became FL Group's main focus. FL Group's acquisitions and corporations were divided into groups, Icelandair Group hf. being one of them and comprising Icelandair, Icelandair Technical Services, Icelandair Ground Services, Loftleiðir-Icelandic and Icelandair Cargo. In February 2006, the board of directors of FL Group announced its intention to list Icelandair Group hf. on the ICEX but postponed it because of unfavourable market conditions. At that time, Air Iceland, Iceland Travel and Icelandair Hotels were transferred to Icelandair Group hf. as were Bluebird Cargo, Icelandair Shared Services, Icelease, IG Invest and Icecap.

In October 2006 three qualified investors, Langflug ehf., Naust ehf. and Ómar Benediktsson founded Icelandair Group Holding hf. with the goal of purchasing Icelandair Group hf. and committed themselves to invest 50.5% of the equity in Icelandair Group Holding. At the same time, Glitnir banki hf. underwrote 49.5% of Icelandair Group Holding as a part of the transaction where Icelandair Group Holding hf. bought Icelandair Group hf. from FL Group. The underwritten shares were sold to groups of qualified investors in October 2006, except 18.5% which were sold, by Glitnir hf., via a share offer, from 27 November to 4 December 2006, to Icelandair Group employees, the general public and qualified investors. Following the share offer, Icelandair Group Holding was listed on the ICEX Main List on 14 December 2006.

On 29 December, 2006 the shareholders of Icelandair Group Holding hf. agreed to the merger of Icelandair Group Holding hf. and Icelandair Group hf. effective as of 1 November, 2006. Following the merger, Icelandair Group will be listed on the ICEX Main List on 12 February 2007 and Icelandair Group Holding delisted after closing on 9 February 2007. The merger is described in detail in the following section.

9.2 MERGER OF ICELANDAIR GROUP HOLDING HF. AND ICELANDAIR GROUP HF.

9.2.1 REASON FOR THE MERGER

Icelandair Group Holding was founded by Langflug ehf., Ómar Benediktsson and Naust ehf., as an acquisition vehicle for the purchase of all shares of Icelandair Group with close to 80% equity and the remainder with debt. The main purpose of having an acquisition vehicle was to reduce the amount of equity required for the purchase of all shares of Icelandair Group.

In the process leading up to the public offer and a listing on the Iceland Stock Exchange, the board of Directors and the Management of Icelandair Group Holding and Icelandair Group came to the conclusion that it would best serve the company and its shareholders if the two companies, Icelandair Group Holding and Icelandair Group were to be merged effective as of 1 November 2006. By doing this, the annual statements of 2006 will best reflect its operational results. With the two companies merged before year end 2006, the statements will reflect the operations for the whole of 2006. This gives investors, creditors and all those who have made significant agreements with Icelandair Group or any of its subsidiaries a better view of the operational results. This is especially important with regards to existing leasing contracts and communications with creditors.

Icelandair Group has made various contracts and guarantees on behalf of its subsidiaries in its normal course of business, while Icelandair Group Holding has not, as it was only established on 15 October 2006. Therefore it was agreed that the shareholders of Icelandair Group Holding would receive shares in Icelandair Group in the merger, and thus Icelandair Group Holding did effectively merge into Icelandair Group.

Both the decision to pursue the merger and the proposed structure of the merger are aimed at benefiting Icelandair Group in its communications with creditors and other intuitions with which it has major agreements and furthermore to best inform investors of the operational results of their investment.

As previously mentioned the merger was approved by shareholders of Icelandair Group on 28 December 2006 and the following day by the shareholders of Icelandair Group Holding or on 29 December 2006.

9.2.2 THE MERGER PLAN

A joint plan[2] dated 15 November 2006 was prepared by the board of directors of Icelandair Group Holding hf. and the board of directors of Icelandair Group hf. concerning the merger of the companies. An assessors' report was also prepared by KPMG for the merger. The merger of the two companies according to this plan was agreed by shareholders meetings of Icelandair Group hf on 28 December 2006 and Icelandair Group Holding on 29 December 2006. The companies were merged under the name of Icelandair Group hf., Icelandic ID No. 631205-1780 effective as of 1 November 2006. Following the merger, the shareholders of Icelandair Group Holding hf. received shares in the nominal value of ISK 1,000,000,000 in Icelandair Group hf., in exchange for their shares in Icelandair Group Holding in the same nominal value.

The only assets of Icelandair Group Holding hf. were shares in Icelandair Group hf. On the day of the merger, Icelandair Group Holding hf. owned shares in the nominal value of ISK 1,000,000,000 in Icelandair Group, i.e. 100% of the shares. The shares were financed 80% with equity and 20% with debt.

On the merger of Icelandair Group Holding hf. and Icelandair Group hf. the former company's shareholders received shares in Icelandair Group hf. in the nominal value of ISK 1,000,000,000 as payment for their shares in Icelandair Group Holding hf. As there were 1,000,000,000 shares in Icelandair Group hf. shareholders received one share in Icelandair Group hf. for every share they held in Icelandair Group Holding hf. before the merger. KPMG hf. acting as advisor on the merger did not find any complications in relations to the merger. Following the merger, Icelandair Group Holding will be delisted and liquidated. Icelandair Group will then be listed on the ICEX Main List.

9.3 NAME AND PLACE OF REGISTRATION AND REGISTRATION NUMBER

The legal name of the Company is Icelandair Group hf. The Company is registered with the Registry of Enterprises in Iceland, under registration number 631205-1780. Icelandair Group domicile and headquarters are at Reykjavík Airport, IS-101 Reykjavík, Iceland, telephone +354 50 50 300. Icelandair Group is a public limited company incorporated in Iceland and operates pursuant to the Companies Act. The date of incorporation is 20 December 2005.

[2] See the Merger plan included in the Appendix. The Merger plan was originally in Icelandic but has been translated to English.

9.4 KEY MILESTONES

1937 Flugfélag Akureyrar founded in Akureyri, on the north coast of Iceland.

1943 Its name is changed to Flugfélag Íslands (Air Iceland) and headquarters moved to Reykjavík.

1944 Loftleiðir (later also known as Icelandic Airlines), is founded.

1945 Flugfélag Íslands makes its first international flights; Loftleiðir follows in 1947.

1953 Loftleiðir pioneers low-fare services across the North Atlantic.

1973 Loftleiðir and Flugfélag Íslands merge to form Flugleiðir.

1979 Flugleiðir assumes operating responsibilities of its two parent companies; Icelandair becomes its international name.

1992 Flugleiðir is listed on the ICEX Main List.

1993 Total renewal of the older aircraft fleet, begun in 1989, reaches a conclusion.

1997 Flugfélag Norðurlands and Flugleiðir's domestic flight operations merge to form Air Iceland (Flugfélag Íslands), a wholly-owned subsidiary of Flugleiðir.

1998 Icelandair Hotels (Flugleiðahótel) founded: the hotels that had been part of Flugleiðir become a distinct subsidiary.

2000 Icelandair Cargo (Flugleiðir Frakt) founded: the cargo business of Flugleiðir becomes a distinct subsidiary.

2001 IGS (Flugþjónustan Keflavíkurflugvelli) founded: Flugleiðir ground services becomes a distinct subsidiary.

2002 Loftleiðir-Icelandic founded: the wet lease and charter arm of Icelandair becomes a distinct subsidiary.

2003 Flugleiðir becomes a holding company with 11 subsidiaries in the travel and tourist industry in Iceland; Flugleiðir's operations are divided into Icelandair, Icelandair Technical Services and Icelandair Shared Services. Icelandair is the largest subsidiary.

2004 Flugleiðir acquires an 8.4% holding in easyJet plc (current ownership is 0%).

2005 Flugleiðir becomes FL Group. The holding company announces its emphasis on investment. This is followed by increased investment activities and the acquisitions of Bluebird Cargo and Sterling Airlines A/S.

2005 Fundamental changes take place in October whereby investments become the focus of FL Group and its airline and tourist service operations are divided between two subsidiaries: Icelandair Group and FL Travel Group.

2006 In February the current structure of Icelandair Group hf. is formed. In 15 October, Icelandair Group Holding hf. is established and at the same day acquires Icelandair Group hf. Icelandair Group Holding is listed on ICEX Main List on 14 December. On 28 December the merger of Icelandair Group Holding and Icelandair Group is approved by the Shareholders of Icelandair Group and the following day by the shareholders of Icelandair Group holding. The Merger is effective as of November 1, 2006.

2007 Icelandair Group Holding is delisted on 9 February and Icelandair Group listed on the ICEX Main List on 12 February.

9.5 PRINCIPAL ACTIVITIES

The object of the Company, according to Article 3 of its Articles of Association, is investment in equity holdings, particularly holdings in other companies engaged in air carrier operations, tourist services and transport operations, buying and selling real estate, credit operations and other related operations.

10 ORGANISATIONAL STRUCTURE

The operation of Icelandair Group is divided into 13 subsidiaries. Each business is managed to create value through strategic and business development decisions. Two subsidiaries play a supporting role: Icelandair Shared Services and Icecap, an insurance company. The other subsidiaries are grouped into three focus areas: Scheduled Airline Operations, Global Capacity Solutions and Aircraft Trading and Travel and Tourism Infrastructure.

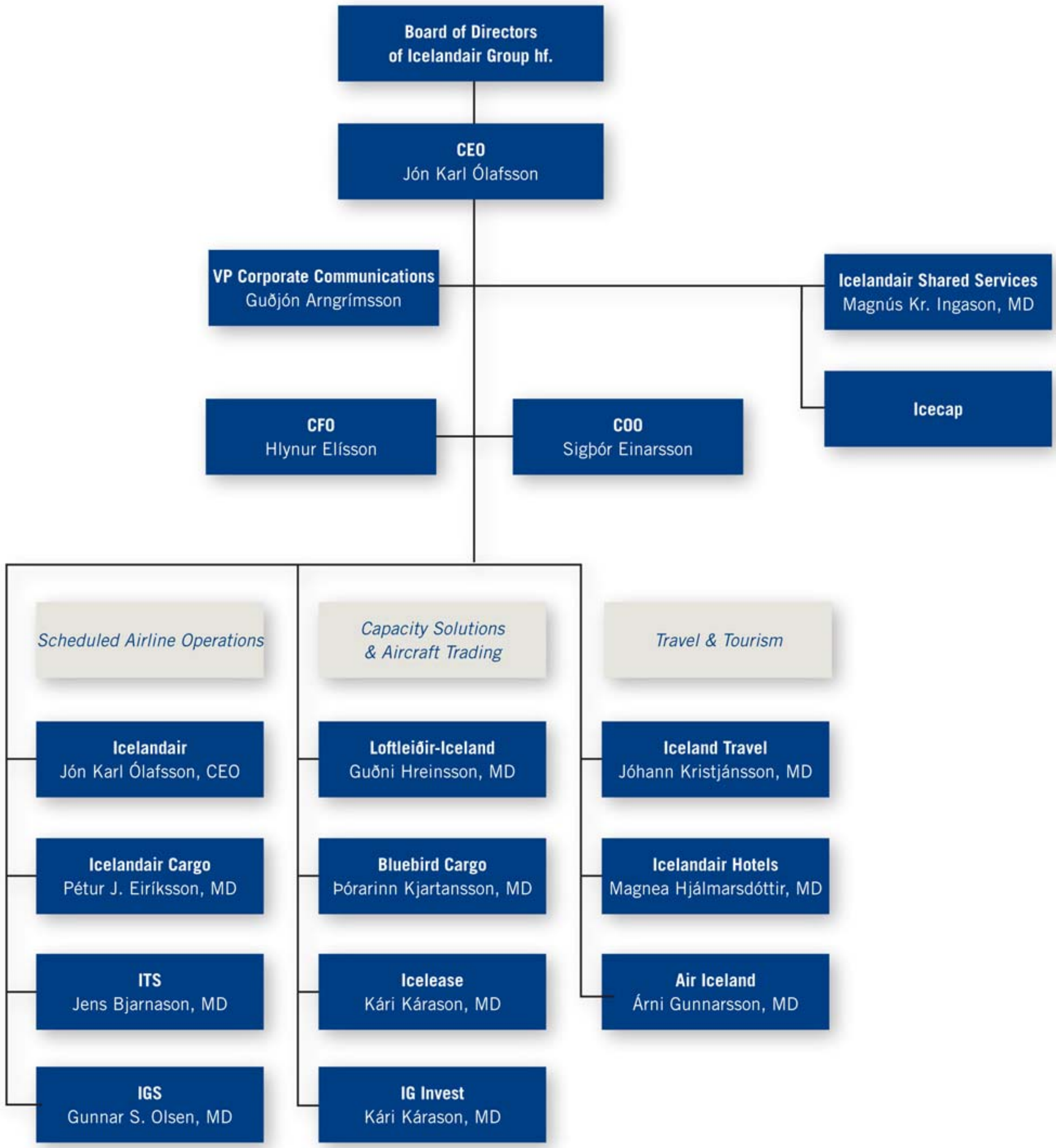

Figure 1. Icelandair Group's organizational structure.

11 SUBSIDIARIES

The most significant subsidiaries of Icelandair Group are listed in
Table 7. The Company does not hold any material stake in other companies. All the subsidiaries are fully owned by Icelandair Group. All the subsidiaries except Icecap are incorporated in Iceland. Icecap is incorporated in the Channel Islands.

Table 7. Subsidiaries of Icelandair Group.

Name	Operations
Icelandair ehf. ID No. 461202-3490 Reg.Office: Reykjavík Airport, 101 Reykjavik, Iceland English brand name: Icelandair	International full service airline with hub in Iceland. Managing Director: Jón Karl Ólafsson Number of employees: 1154
Flugþjónustan Keflavíkurflugvelli ehf. ID No. 551200-3530 Reg.Office: Heiðarból 43, 230 Reykjanesbær, Iceland English brand name: Icelandair Ground Services (IGS)	Ground handling for airlines and passengers at Keflavik Airport. Managing Director: Gunnar S. Olsen Number of employees: 522
Tækniþjónustan á Keflavíkurflugvelli ehf ID No. 511202-2990 Reg.Office: Keflavíkurflugvöllur, 235 Keflavíkurflugvöllur, Iceland English brand name: Icelandair Technical Services (ITS)	Maintenance and technical services for Icealndair and otherairlines. Managing Director: Jens Bjarnason Number of employees: 260
Flugleiðir-Frakt ehf. ID No. 471299-2359 Reg.Office: Reykjavík Airport, 101 Reykjavik, Iceland English brand name: Icelandair Cargo	Low asset transportation company, leasing and outsourcing space, handling and sales. Managing Director: Pétur J. Eiríksson Number of employees: 50
Loftleiðir-Icelandic ehf. ID No. 571201-4960 Reg.Office: Reykjavík Airport, 101 Reykjavik, Iceland English brand name: Loftleiðir-Icelandic	Capacity provider for the international airline and tour operator industry. Managing Director: Guðni Hreinsson Number of employees:11
Bláfugl ehf. ID No. 460899-2229 Reg.Office: Hlíðarsmári 15, 20 Kópavogur, Iceland English brand name: Bluebird Cargo	Transportation services provider. Fleet of freighter aircraft. Air cargo sales agency. Managing Director: Þórarinn Kjartansson Number of employees: 64
Icelease ehf. ID No. 670505-0140. Reg.Office: Reykjavík Airport, 101 Reykjavik, Iceland English brand name:Icelease	Buying, selling and leasing of aircraft. Arrangement of aircraft trading transactions. Managing Director: Kári Kárason Number of employees: 1
Flugfélag Íslands ehf. ID No. 530575-0209. Reg.Office: Akureyri Airport, 600 Akureyri, Iceland English brand name: Air Iceland	Sceduled domestic carrier. Flights to Faeroes and Greenland. Managing Director: Árni Gunnarsson Number of employees: 282

Name	Operations
Flugleiðahótel ehf. ID No. 621297-6949 Reg.Office: Reykjavík Airport, 101 Reykjavik, Iceland English brand name: Icelandair Hotels	Markets and operates two hotel chains. Managing Director: Magnea Hjálmarsdóttir Number of employees: 263
Íslandsferðir ehf. ID. No. 410791-1379 Reg.Office: Lágmúli 4, 108 Reykjavík, Iceland English brand name: Iceland Travel	Tour operator and travel agency in incoming tourism. Managing Director: Jóhann Kristjánsson Number of employees: 48
Fjárvakur-fjármálaþjónusta ehf. ID. No. 521202-2620 Reg.Office: Reykjavík Airport, 101 Reykjavik, Iceland English brand name: Icelandair Shared Services	Financial services for Icelandair Group Managing Director: Magnús Ingason Number of employees: 77
Icecap Insurance PCC limited Reg.Office: Polygon Hall PO Box 225 Marchant Street St. Peter Port Guernsey GY 4HY Channel Islands English brand name: Icecap	Insurance services for Icelandiar Group.
IG Invest ehf. ID. No. 490905-0730 Reg.Office: Reykjavík Airport, 101 Reykjavik, Iceland English brand name: IG Invest	Holding company managed by Icelease. All operations covered by Icelease.

12 ICELANDAIR GROUP

Icelandair Group owns 13 independent subsidiaries. The largest subsidiary is the international airline Icelandair, which accounts for approximately 53% of the Group's turnover as of 30 September 2006. Other companies are Icelandair Technical Services, Icelandair Ground Services, Lofteiðir-Icelandic, Icelandair Cargo, Bluebird Cargo, Air Iceland, Iceland Travel, Icelandair Hotels, Icelease, IG Invest, Icelandair Shared Services and Icecap. Icelandair Group is an international service and trade company, with firm roots in Iceland. On 31 December 2006 the Company employed 2,747 people.

The management of Icelandair Group is led by Jón Karl Ólafsson, Chief Executive Officer of Icelandair Group and Icelandair. The goals for the corporate management within the Group are to increase shareholder value, harnessing the potential synergy effects, to organise overall operational network, to ensure efficient financial management and to push the overall strategy. All operational companies of the Group have their individual management with executives in charge of the daily business, supported by the Group management. To enhance the Group's performance further, it has been structured in three main areas of focus:

- Scheduled Airlines Operations
- Global Capacity Solutions and Aircraft Trading
- Travel and Tourism Infrastructure

The airline, transportation and tourism sectors are expanding both in and around Iceland and throughout the world, and Icelandair Group has the means to participate actively in this dynamic market. All areas present opportunities for both organic and acquired growth. Icelandair's route network, which forms the basis of the Group's scheduled airlines operations, has grown in recent years and has the potential to grow further into international markets. Cargo and charter operations have achieved an even faster growth rate within Icelandair Group in recent years. Travel services within Iceland have been growing steadily; the current situation is good and the number of tourists travelling to Iceland is growing. Icelandair has a long history of successful trading with aircraft that has been gaining momentum through the incorporation of Icelease and IG Invest and the numerous aircraft trades that have been handled during the last 18 months. In general, Icelandair Group has developed a healthy business which generates more than 70% of its revenue outside Iceland.

Icelandair Group has earned profits in recent years by achieving improved operating efficiency and cost control, focussed distribution, marketing, sales and revenue management, and has shown strength in a time that has been volatile for many airline-related industries. The company has a workforce of considerable experience and expertise in the airline, transportation and tourism sectors, which is a prerequisite for running a profitable business in a very competitive environment. Throughout its long history, the company has consistently been able to renew itself and adapt to change, and this has been one of its key strengths. In the management's opinion, the Company has the ability to expand, both in Iceland and internationally.

12.1 SCHEDULED AIRLINE OPERATIONS

Four companies are categorized as being part of the Scheduled Airline Operation focus of the group: Icelandair, the international full-service airline with a hub in Iceland; Icelandair Cargo, a full-service air-freight company; Icelandair Ground Services, which handles airlines and passenger services at Keflavik Airport and Icelandair Technical Services, which provides maintenance for Icelandair and other airlines. These companies work closely together and have long historical ties. In 2005 they represented roughly 65% of the Group's income according to the Pro Forma Income Statement.

Their main common task is to run a profitable airline network operation with growth potential. This is done by sales and marketing activity on behalf of all companies, as well as putting emphasis on revenue management and cost control throughout the operation.

12.1.1 ICELANDAIR

Purpose of the company

Icelandair is the largest subsidiary of Icelandair Group. The purpose of company is to be a profitable international full-service airline which offers its customers quality service. In 2005, Icelandair carried about 1.5 million passengers; during the first nine months of this year the figure was 1.2 million. In 2006 the company has offered daily scheduled flights from Iceland to Europe and North America to a total of 22 destinations. The company operates a fleet of 12 aircraft for its scheduled operations.

History

As an airline, Icelandair traces its roots to the year 1937, when Flugfélag Akureyrar was founded in Akureyri on the north coast of Iceland. In 1943 the company moved its headquarters to the capital, Reykjavík, and changed its name to Flugfélag Íslands, which later assumed the international brand name Icelandair.

Another important milestone was passed in 1944, when three young Icelandic pilots, returning from flight training in Canada, founded Loftleiðir, later also known as Icelandic Airlines. Initially, both companies concentrated on Icelandic domestic air services. However, in 1945 Flugfélag Íslands made its first international flights, to Scotland and Denmark. Loftleiðir began international operations in 1947, and its pioneering low-fare services across the North Atlantic commenced in 1953.

In 1973 Flugfélag Íslands and Loftleiðir merged under a new holding company named Flugleiðir. In October 1979 Flugleiðir assumed all operating responsibilities of its two predecessors, and decided to use Icelandair as its international brand name, retaining the name Flugleiðir only in the Icelandic domestic market. On the 50th anniversary of the company in 1987, a breakthrough agreement was signed with Boeing to renew Icelandair's international aircraft fleet and a new route network was established. A new generation of Boeing jets, Boeing 757-200s and 737-400s, replaced the older fleet gradually from 1989 to 1993, and then a single-type fleet of Boeing 757s was established in the years preceding 2003.

In 1997, Flugfélag Norðurlands and Flugleiðir's domestic flight operations were merged to form Air Iceland, a wholly-owned subsidiary of Flugleiðir. Loftleiðir-Icelandic was founded in 2002 when the wet-lease and charter arm of Flugleiðir became a distinct subsidiary. In January 2003, Flugleiðir became a holding company with 11 subsidiaries in the travel and tourist industry in Iceland. At that time the company that handles international airline operations was named Icelandair.

Icelandair has been a member of International Air Transport Association (IATA) since 1950, a member of the Association of European Airlines (AEA) since 1957, and a member of the Flight Safety Foundation (FSF) since 1966.

Management

Icelandair's management team has years of experience with the company and within the industry. Jón Karl Ólafsson is the CEO of Icelandair ehf.

Gunnar Már Sigurfinnsson

Gunnar Már Sigurfinnsson is the Senior Vice President (SVP) of Sales and Marketing. Gunnar Már was appointed his current position in March 2005. He started at Icelandair Domestic in Vestmannaeyjar, the islands off the south coast of Iceland, in 1986 and in 1994 he became sales and marketing manager for Air Iceland. In 1997 he became the sales manager for Icelandair in Germany, based in Frankfurt. Gunnar Már became Director of Sales

Planning and Control in 2000 and in 2001 he became General Manager of the Germany, Netherlands & Central Europe region.

Andri Áss Grétarsson

Andri Áss Grétarsson is the SVP of Finance and Resource Management. Andri was appointed to his current position in April 2006. He joined Flugleiðir in 1998, first in the Management and Financial Information department and then worked in the Strategic and Finance division at Flugleiðir. He holds a Cand.Oceon degree from the University of Iceland, and has worked in accounting since 1993.

Guðmundur Pálsson

Guðmundur Pálsson is the SVP of Flight Operations. Guðmundur was appointed to his current position in 1996. He joined Flugleiðir in 1974, and served initially in the Budget and Long Range Planning Department. In 1980 he became Director of Cash Management and Insurance, serving in that position until 1986 when he was appointed SVP Operations, in which capacity he worked until 1988, when he was appointed SVP Technical.

Una Eyþórsdóttir

Una Eyþórsdóttir is the VP of Human Resources. Una was appointed her current position in 2001. She joined Flugleiðir in 1975, first in Human Resources, from 1983 to 1987 in Information Technology department, first as a supervisor and later a divisional manager, and then in Information department 1987-1996 as a divisional manager. She was appointed manager of Employee Development in 1996 and Personnel Manager in 2001. Una studied English and Psychology at the University of Iceland and earned an MBA degree from the same university in 2002.

Hjörtur Þorgilsson

Hjörtur Þorgilsson is the VP Information Technology. Hjörtur was appointed his current position in January 2006. He joined Flugleiðir in 1985, started in Technical department's cost control unit, became divisional manager in the Planning Department 1988 and Manager in 1994, and then Manager of the Information Development in 1997. Hjörtur received his Cand.Oceon from the University of Iceland in 1985.

Operation

Icelandair uses the location of Iceland in the North Atlantic between North America and Europe as the key to the company's network strategy and operations. By using Keflavik International Airport as a hub, it serves three market segments, i.e. customers travelling from Iceland, customers travelling to Iceland and customers crossing the Atlantic via Iceland. By tuning and adding to this network over two decades the company has multiplied the frequency of trips to and from Iceland – and thus formed the foundation of the Icelandic travel and tourism industry, and at the same time offered the population of Iceland (300,000) more air travel destinations than it sould otherwise be able to sustain in terms of its size.

The design of Icelandair's network allows the company to increase its product offering considerably. For example, by enabling passengers to catch a connecting flight in Iceland, a flight arriving from the USA not only carries passengers who are going to Iceland but also passengers heading for other European destinations served by Icelandair.

Owing to this network structure, Icelandair is able to offer flights on a wider variety of routes than the number of destinations implies. By matching US flights with European flights, Icelandair is able to offer flights on 54 routes in the winter and 89 during the summer, with 14 and 22 routes from Iceland respectively.

As of summer 2007, Icelandair will introduce a new Bank into the Route Network. By introducing the new Bank Icelandair is improving its product in all three markets, To, From and Via Iceland, by offering flights at times that it has not covered in the past years and increase frequency to Scandinavia and North America. The new Bank offers the following addition to the Route Network: Early morning departures from Scandinavia (Copenhagen, Stockholm and Oslo) to Keflavik and late morning departures to North America (Boston and New York) from Keflavik. Afternoon departures from North America (Boston and New York) to Keflavik and night departures from Keflavik to Scandinavia (Copenhagen, Stockholm and Oslo). Therefore, the new Bank will not only offer additional operating times between Iceland. North America, and Scandinavia: it will also give Icelandair customers the option of travelling between Scandinavia and North America via Iceland at times that have not been offered in the past.

Flight operations

In additon to aircraft flown on Icelandair's scheduled network, Icelandair Flight Operations operates aircraft on behalf of Loftleiðir-Icelandic ehf. and Icelandair Cargo ehf., thus securing large economies of scale. Icelandair's network has mostly been served by eight to ten Boeing 757 aircraft and one Boeing 767-300ER, while the Loftleiðir-Icelandic contract includes four Boeing 757s and two Boeing 767s. Five Boeing 757 cargo aircraft are operated on behalf of Icelandair Cargo. Icelandair has ordered and confirmed four Boeing 787 aircraft – Dreamliners – for delivery in 2010-12. The airline has also confirmed options for three more such aircraft, for possible delivery in 2012-2013. These new aircraft will open up new markets for the airline, as the range will be extended to almost the whole world. At the same time, these new aircraft will be state-of-the-art technically, more efficient, with lower fuel consumption and lower maintenance costs. The airline is considering options regarding the replacement of the Boeing 757 fleet in 7-12 years' time.

In January 2007, Icelandair signed an agreement to purchase a new in flight entertainment system. The entertainment system will give passengers access to a broad selection of new movies, TV programs, music, books, e-magazines and games. In addition to this the technology enables the passengers to download and buy music and other digital products such as computer games as well as ordering various goods and services at their destination. At the same time the passengers can monitor the flight and get information about airports, departures, arrivals and etc. Some of these services will be free of charge for passengers, but the new technology also opens considerable revenue possibilities for Icelandair.

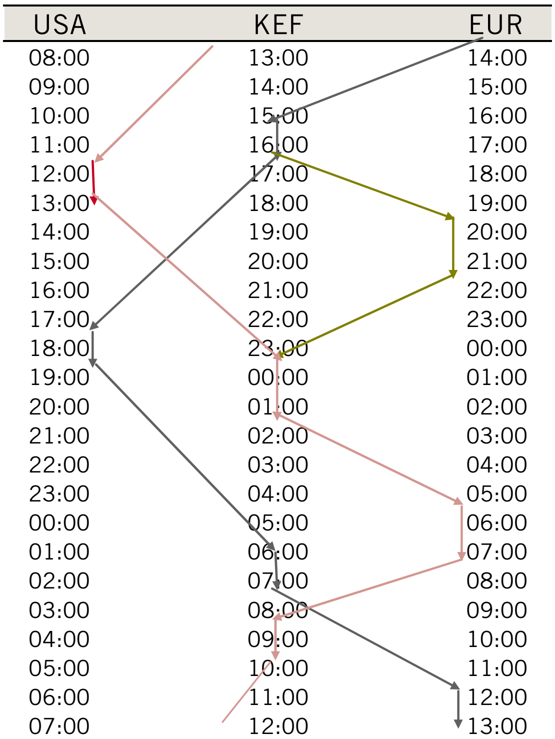

Figure 2. Icelandair's route network as of summer 2007

The company has also singed an agreement to purchase new seats for Icelandair's fleet.The new seats and the in flight entertainment system will be installed in all of Icelandair's Boeing 757 passenger aircraft that are used for the company's scheduled routes. The renewal will start in the fall of 2007 and end in the spring of 2008.

Icelandair's crews are experienced and are considered one of the many assets of the company. Initial pilot training is mostly done in-house, but simulator training is done in various places, mostly in Europe. Iceland has a long aviation history, and Icelandair employs experienced aviators. Icelandair's current union agreements with its pilots and cabin attendants are valid until the end of 2007.

Sales and marketing

For an Icelandic company, Icelandair is unique for its decades of experience in selling its products globally on the general consumer market. Among airlines, Icelandair has an unusually high percentage (70%) of its customers outside its home market.

Icelandair is a full-service airline which offers its customers a variety of services related to air travel, but has, like many other airlines, categorized these services into two key products, Saga Business Class and Economy Class. Icelandair reaches its customers through four main channels:

1. Own sales offices
Icelandair runs its own sales offices in key markets, i.e. Iceland, the USA, the UK, Denmark, Sweden, Norway, Finland, France, Holland, Germany, Spain and Italy. The biggest of these offices are in Iceland, the USA, the UK and Denmark. The role of the sales offices in selling tickets to customers has decreased, but they still play an important role in customer relations, especially with corporate clients and larger groups and as a foundation for marketing and sales activity in each market. Icelandair has general sales agents in 28 countries of which eight are in the Far East.

2. Telephone call centres
Icelandair operates call centres in its key markets with staff speaking local languages, and connects these call centres so that when all lines are busy in one country, calls can be transferred to another.

3. Travel agents
Icelandair products are sold by leading travel agents, tour operators and airlines all over the world through various contracts and agreements to which Icelandair is a party. Icelandair uses the Amadeus CRS system which enables travel agents to book tickets in their offices or websites with Icelandair simultaneously. In 2005 about 12,000 agencies sold tickets with Icelandair.

4. Internet
Icelandair has web sites in local languages in all its key markets and an increasing number of tickets are sold through the internet, both on Icelandair's own websites and the websites of others. Icelandair has a net club of about 543,000 active members, who receive special offers and information on a regular basis.

Revenue management and distribution
The foundation of the distribution of Icelandair's products throughout the world is its partnership in the Amadeus booking and distribution engine, and numerous interline agreements with other leading airlines. This makes it possible for Icelandair to sell its products simultaneously all over the world through millions of computer screens, telephone call centres, offices and websites. For example, the last three available seats on a particular flight can be sold at the same time, one through an agent in China, one through the internet in Kansas and one at the sales office in Copenhagen. In all instances the financial transaction can be concluded and everyone involved will then know that this particular flight is full. At the same time, Icelandair can sell airline tickets and other services with airlines and service providers in all parts of the world.

A key ingredient of a successful airline is its revenue management, the strategy of maximizing revenue by controlled booking and pricing. Icelandair has used proven airline systems and methods in this field; since the end of September it has used a new and more advanced revenue management system from PROS, a world leading provider of revenue management systems. Improvements have also been made to Icelandair's revenue integrity system, the purpose of which is to locate and cancel false bookings automatically, with evident revenue benefits. Revenue management is most effective during strong demand periods. These implementations should therefore yield significant revenue improvements during the next peak demand period, in the summer of 2007.

The company's load factor follows the seasonality in demand. Icelandair operates more aircraft during the high season and the load factor is highest during the summer peak. The company had an average load factor of 77.8% for the first nine months this year, compared to 77.6% for the whole year 2005, which in turn represented an improvement over the 75.4% load factor during 2004. This is in line with the increase in the break-even load factor, which grew by 1% from 2004 to 2005. The break-even load factor is the balance point between the average seat price and the load factor needed for the airline to break even. The company controls the break-even load factor by managing its seat price and availability. Icelandair has successfully improved its load factor at the same time as the number of flights rose considerably.

Market and current market position

Icelandair defines its customer base in terms of three main markets:

- Passengers from Iceland (about 28% of passengers)
- Passengers to Iceland (about 36% of passengers)
- Transatlantic passengers travelling via Iceland (about 36% of passengers)

Passengers from Iceland

There has been strong demand for air travel from Iceland recently. On most of its routes from Iceland the company is the only airline operating. For most business travellers Icelandair is the only option in terms of the frequency of flights and the number of destinations. The Icelandair frequent flyer program (Vildarklúbbur), which has over 100,000 members in Iceland, also helps attract business travellers. The company's pricing policy is designed to capture some of the value that business travellers see in being able to schedule their trip at short notice and return promptly. Icelandair's revenue from passengers from Iceland has grown by 15-20% annually for the last 3 years.

Passengers to Iceland

Iceland has enjoyed increasing popularity as a tourist destination over the past 25 years. The number of tourists visiting Iceland grew from 72,194 in 1981 to 369,400 in 2005 according to ITB immigration figures[3], which is an increase of 7.0% annually. Over this time the vast majority of the tourists have travelled to Iceland by Icelandair. The company has fuelled this increase by the establishment and development of a network with a very high frequency of flights to Iceland and by strong marketing efforts in Europe and United States. Tourists visiting Iceland come from several economic areas, which makes the company less sensitive to the economy in the areas of specific destinations; if there is a slowdown in one destination the company can reduce the frequency of flights and increase the capacity in another market area instead.

Transatlantic passengers travelling via Iceland

The transatlantic market is the second largest air travel market in the world after the US domestic market, and ahead of the western European market measured in revenue passenger kilometres, according to the International Air Transport Association. Revenue passenger kilometres are computed by multiplying the total number of paying passengers by the kilometres they have flown. The market over the Atlantic was deregulated in the 1990s, which resulted in reduced fares, stimulated new traffic and shifted traffic more into the hub-and-spoke system rather than point-to-point. Icelandair's main focus is on city pairs between which there are limited direct flights. The transatlantic market is growing, and Boeing Market Outlook[4] forecasts that this market will grow 4.6% annually over the next 20 years.

Icelandair's strength in crossing the Atlantic lies in the company's network utilizing the geographical position of Iceland on the flight route between Europe and the eastern shore of the USA. The North Atlantic market is very competitive, with numerous market players. Due to this, Icelandair faces fierce competition in pricing, especially in winter time (low season). Icelandair's market share on the North Atlantic market is below 1%. On routes where the company is competing with direct flights and over-capacity, it has no pricing power and tries to concentrate on customers in other areas instead. The North Atlantic market helps Icelandair to operate efficiently. Due to the immense size of this market and the nominal market share by Icelandair, the market virtually serves as a gigantic reservoir of passengers. Access to this market is essential for the company to be able to maximize its yield. When it encounters difficulties in selling the seats on a flight to passengers who are travelling to and from Iceland, the

[3] These figures can be found on the website http://www.ferdamalastofa.is/displayer.asp?cat_id=503

[4] The Outlook can be found on the website http://www.boeing.com/commercial/cmo/

company is able to offer competitive prices on the North Atlantic market and obtain revenue from seats that would otherwise be empty.

Due to the nature of the North Atlantic market and the marginal market share of Icelandair, the North Atlantic market serves as a buffer. If, for some reason, there were to be a slow-down in the markets for travel by air to and from Iceland, the proportion of passengers from the North Atlantic market would grow, and vice versa. Icelandair has many options to expand its network, for example by flying further east and thereby offering flights from the USA and Europe to Asia with a short stopover in Iceland.

Competition

Icelandair faces competition in all its markets and always has done; however, the company has shown the ability to grow and profit in this competitive environment. Furthermore, history shows that increased capacity has increased the overall market size, as there are more contact points with customers.

Icelandair is by far the largest operator offering flights between Europe and Iceland. It is the only airline that offers scheduled flights between Iceland and North America. The company is the market leader in flights to and from Iceland with a market share of about 59%, according to the management's estimates. Based on this, the management believes that Icelandair is well positioned to meet the increased competition in the market, and it sees an opportunity for Iceland as a travel destination to tap into the large customer base of the foreign airline operators entering the market periodically.

Even though most of Icelandair's passenger traffic is leisure traffic, with only about 15% being "must go" business traffic, it has tripled its passengers numbers over a 15-year period. Operating on different and independent passenger markets (The North Atlantic market, From Iceland market and To Iceland market) gives the company more options when allocating the number of available seats on routes and deciding on price strategy. Apart from marketing and sales efforts, demand for air travel mainly depends on the economy, exchange rates, destination popularity and the cost of flying. Operating in variable markets makes the company less vulnerable to fluctuations in demand for any particular market segment.

In all its markets, Icelandair's destinations and products are in direct competition with other destinations and products. A customer in London contemplating a "city-break" can choose a four-day trip to Reykjavik, but he can also pick a large number of other cities in all European countries with numerous airlines and tour operators offering very similar packages. In Iceland, customers looking for summer vacation trips abroad have a wide variety of options other than the 22 Icelandair destinations, such as the many offers from travel agencies using charter, and scheduled flights of other airlines. Despite this competition, Icelandair has been growing at a steady pace and the market has been growing in general due to increased availability of air transport to and from Iceland. This total growth of the market has enabled growth for the players on the market without direct conflict over market shares.

According to the management of Icelandair the company's main competitors in Iceland are Express ferðir ehf. (Iceland Express) and charter operators. Express ferðir ehf. is part of Northern Travel Holding hf. which also holds all of the shares in the Danish low cost carrier Sterling Airlines AS, 51% of the UK based charter airline Astraeus Ltd., 29.26% of the listed Swedish travel agent Ticket AS and all of the shares in Danish travel agent Hekla Travel AB[5]. Express ferðir ehf. is a marketing vehicle that leases aircraft from a wet-lease operator and has recently announced expansion to its current network of destinations for scheduled flights. Express ferðir ehf. offers daily flights to London and Copenhagen and flights up to two times a week to Alicante, Berlin and Frankfurt Hahn. This

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http://news.icex.is/newsservice/MMIcexNSWeb.dll/newspage?language=IS&pagetype=symbolnewslist&primarylanguagecode=EN&newsnumber=36359

summer, Express ferðir ehf. increased its number of flights and offered flights to a total of eight destinations. Express ferðir ehf. is planning to fly to a total of 14 destinations in Europe during the summer of 2007.

Two airlines started scheduled flights to Iceland this summer. British Airways Plc. flew five times a week between Gatwick and Keflavik until the end of September, when the number of flights was decreased to four. The flight leaves Gatwick at 7:30 in the morning, which indicates that the schedule is more geared towards the needs of passengers travelling to Iceland than passengers who begin their journey in Iceland. SAS Braathens AS started flying from Oslo to Iceland three times a week in March 2006. Both airlines will continue flying to Iceland, with SAS Braathens AS also offering scheduled flights between Stockholm and Keflavik.

Icelandair's market share on the market to and from Iceland was not affected by increased number of flights in 2006 and it seems that the rivals' market share was mainly at the expense of charter flights.

Like the number of Icelandair's international passengers, the number of passengers who pass through Icelandair's hub in the past 20 years has more than tripled. The management of Flugstöð Leifs Eiríkssonar hf. (Leifur Eiríksson International Air Terminal) has had BAA conduct a 10-year traffic forecast, which predicts that the traffic will grow to 3.2 million passengers by 2015. Currently contractors are enlarging the hub to be better positioned to serve the expected increase in the number of travellers.

Icelandair's competitive position has been strong in the past few years. The company has been profitable when the industry in general has been struggling. It has effectively worked on reducing its fixed costs, which makes it more competitive in today's aviation market. It is now more flexible and can more effectively add or reduce capacity depending on market conditions.

Future strategy

Icelandair aims to continue to grow and improve its current scheduled-passenger network. The new Hub planned for the summer of 2007 forms part of this future strategy. The company's focus over the next few months will be on simplifying processes and products and reducing unit costs within the business model as it is today. The company is constantly optimizing the network and looking at new markets. The Boeing 767 and later the Boeing 787 will open up new growth opportunities for the company in more distant markets, e.g. Asia.

12.1.2 ICELANDAIR GROUND SERVICES (IGS)

Purpose of the company

Icelandair Ground Services provides comprehensive airport ground handling services for airlines and passengers at Keflavík International Airport.

History

IGS was formed in 2001, but airport and ground operations in Iceland have been a part of the airline operation from the foundation of Icelandair Group predecessors.

Management

Gunnar S. Olsen

The Managing Director of IGS is Gunnar S. Olsen. Gunnar was appointed Managing Director when an independent company was formed to handle Icelandair's ground services in Keflavík in 2001. He has held various managerial positions within Icelandair Group hf. in Iceland and abroad.

Operation

IGS provides aircraft ground handling services for all types of aircraft, a first-class flight kitchen and bonded stores, a new state-of-the-art cargo centre and a restaurant division in the Leifur Eiriksson Air Terminal. All these units are organised and settled as profit units.

Market and current market position

IGS is a service provider enabling airlines and other customers to obtain all services required through one service provider. IGS competes with two other suppliers of ground handling services at Keflavík Airport. The company has been profitable throughout its history, with the exception of the year of foundation (2001). Icelandair is by far the biggest client of IGS, but the company has been contracting with other airlines as well.

Future strategy

IGS has contracts with most airlines using Keflavik Airport and aims to maintain its market share. Opportunities for growth go hand in hand with the expected growth in the number of passengers passing through the airport.

12.1.3 ICELANDAIR TECHNICAL SERVICES (ITS)

Purpose of the company

Icelandair Technical Services' core business is to provide Icelandair Group and its subsidiaries with high-quality maintenance and technical services. However, it is planned to merge ITS back into Icelandair, at the end of this year, as a profit centre to simplify the operational processes further.

History

Icelandair Technical Services began operations at the end of 2002; before becoming an independent subsidiary it was a part of Icelandair.

Management

Jens Bjarnason

The Managing Director of ITS is Jens Bjarnason. Jens was appointed to his current position on 20 September 2005. He joined Flugleiðir in September 1996 as Director of Flight Operations after working for the Icelandic CAA as Director of Flight Safety. He is an aeronautical engineer and received his Ph.D. from Northwestern University in the USA in 1992.

Operation

ITS provides aircraft maintenance and technical services for Icelandair, Loftleiðir – Icelandic and Icelandair Cargo. The company also provides services to aircraft that land in Keflavík, heavy maintenance in Keflavík and technical services for several operators. It is also active in maintenance at several locations abroad.

Market and current market position

ITS is Iceland's largest company within its field, operating a first-rate maintenance centre for aircraft in Iceland. The market in Iceland has been growing, as Icelandair has increased its operations every year. However, the company is also an experienced Boeing 757 service provider and has offered its services to other such operators in cooperation with Volvo and British Airways Maintenance – called the Team 757. This is a new service, but it has already created some interest in the market.

Future strategy

In the near future, ITS will be merged into Icelandair ehf., as part of which it will concentrate on growth with Icelandair Group and its subsidiaries, as the plans for increased numbers of aircraft call for growth at ITS.

12.1.4 ICELANDAIR CARGO

Purpose of the company

Icelandair Cargo is a low-asset company, leasing aircraft and buying capabilities from other sources. The freighters are placed on Icelandair´s air operating certificate and crews are leased from Icelandair. Aircraft maintenance, warehousing, cargo handling and part of cargo sales are outsourced.

History

Icelandair Cargo was established in late 1999, though cargo transport had been a part of the airline’s core business since its foundation. Icelandair Cargo is the largest air freight service provider in Iceland.

Management

Pétur J. Eiríksson

The Managing Director of Icelandair Cargo is Pétur J. Eiríksson. Pétur was appointed to his present position in January 2000. He joined Flugleiðir in June 1981 and has held several positions within Icelandair, including Director for Scandinavia and Finland, Senior Vice President of Marketing and Senior Vice President of Business Development before taking over his present position when Icelandair Cargo was founded. Pétur holds a B.Sc degree in economics from the University of Edinburgh and a master’s degree from the University of Gothenburg, Sweden.

Operation

The company bases its business on scheduled services between Iceland, Europe and North America supported by charters and wet leases (aircraft, crew, maintenance and insurance). In addition to marketing and selling space on its own freighters, Icelandair Cargo sells the cargo hold space on Icelandair´s passenger aircraft. Icelandair Cargo has five Boeing 757-200 freighters in its fleet. There are nine flights per week to Liege in Belgium, four to Brussels, four to Humberside in the UK, and one to the East Midlands, two to Jönköping and one to Malmö in Sweden. In North America, New York, JFK is served six times per week, and Charlotte, NC and Halifax in Canada once per week. This network of freighter aircraft is enhanced with 22 destinations in the Icelandair passenger network. Icelandair Cargo has 58 employees, most of whom are in sales and marketing, finance and freight operations.

Market and current market position

Icelandair Cargo offers its customers competitive and quick global services through extensive interline and special pro-rate agreements with other airlines. The company also operates trucking network in Europe and by demand in the USA. Sales are made by its own staff in Iceland, the Benelux countries and North America and by general sales agents (GSAs) in other markets. The company has a number of GSAs in all of the larger or growing markets Asia and in most countries in Europe.

In 2006 the management of Icelandair Cargo expects the company to carry 39,000 tons, of which 20,000 are expected to be exports from Iceland, 11,000 imports and 8,000 tons moved between Europe and North America. Eighty-five per cent of the exports consist of fresh seafood, whereas the imports are produce, high-tech products and spare parts. There was a sharp decline in fish exports from Iceland in 2005 due to currency issues, with serious consequences for the company’s bottom line. For a number of years, Icelandair Cargo has carried express freight for TNT to Iceland and over the Atlantic, and it also counts DHL and FedEx as among its most important customers.

Future strategy

The management of Icelandair Cargo is expecting to increase the company’s turnover over the next five years, partly through growth in existing markets but mainly through extension into other geographical areas. This calls for larger and longer-range aircraft than the Boeing 757-200. Current analysis is mainly centred on the Boeing 767-300 or Boeing 777-200.

12.2 GLOBAL CAPACITY SOLUTIONS AND AIRCRAFT TRADING

The four companies forming this part of the Icelandair Group are Loftleiðir-Icelandic, a capacity provider for the international airline and tour operator industry, Bluebird Cargo, a transportation services provider and Icelease, which handles the buying, selling and leasing of aircraft using IG Invest as its holding company.

The four companies are grouped together to emphasize Icelandair Group's increased focus on international expansion in this field. Their role is to capitalize on internal know-how by offering aircraft operation services to third parties and taking advantage of trading opportunities in a fast-growing world market, as well as looking for opportunities for mergers and acquisitions.

12.2.1 LOFTLEIÐIR – ICELANDIC

Purpose of the company

Loftleiðir–Icelandic is a capacity solution company for the international passenger airlines and tour operator industries.

History

Loftleiðir-Icelandic was formed as a subsidiary of FL Group in 2002, though international charter operations had been a part of the general operations of the airline and its predecessors for decades. It has developed from being a marketing vehicle operating in the international ACMI (Aircraft Crew Maintenance and Insurance) and charter markets, to become a capacity solution provider, thus expanding its horizon above the aircraft types traditionally operated under the Icelandair AOC. In early 2006, the company bought a majority of the shares in the Latvian charter operator LatCharter Airlines as part of Loftleiðir-Icelandic´s strategy to strengthen its position in the Baltic and CIS region and add the Airbus family into its worldwide ACMI product line.

Management

Guðni Hreinsson

Guðni Hreinsson took over as Managing Director of Loftleiðir-Icelandic in 2006. Guðni joined Flugleiðir in 1997 as a marketing representative in Sales Control and from 2000-2003 he worked at The Icelandic Web Agency. Since 2003 Guðni has been Director Marketing at Loftleiðir-Icelandic. Guðni holds a Bachelor's degree in Humanistic Informatics & Communication from Aalborg University, Denmark.

Operation

The company currently operates AM (aircraft and maintenance), ACMI (aircraft, crew, maintenance and insurance) and full charter contracts in Europe, Africa, the Middle East and North and South America. Furthermore Loftleiðir-Icelandic has established itself as a business class operator serving one of the most prestigious operators in the USA, A&K (Abercrombie & Kent), by operating first-class flights around the world on which all seats are business class. The company has five Boeing 757-200 and three Boeing 767-300ER aircraft, all but one of which are operated under Icelandair's AOC (Air Operator's Certificate). In addition, the company has two Airbus 320 aircraft, operated under the LatCharter Airlines AOC.

Market and current market position

Current market conditions are favourable especially on the wide-body market due to a lack of aircraft availability. Thus, the wide-ranging aircraft market knowledge accumulated within Loftleiðir-Icelandic has put the company in a good position to meet demand. In mid-2003, the company added the first wide-body aircraft by introducing a Boeing 767 to its fleet, which opened up new markets. This led to an increase in the proportion of ACMI projects at the expense of all-inclusive projects, which has helped to increase profitability and reduce sensitivity towards external fluctuations.

The company has had success in establishing itself on the European market and enjoys increasing awareness in both the North- and South American markets. Furthermore, the company has been eyeing the CIS (Commonwealth of Independent States) market for future growth; this formed the basis for the purchase of LatCharter.

Future strategy

Loftleiðir-Icelandic currently seeks to use its extensive market knowledge to widen its spectrum of services further, so that continued growth in revenue and profitability can be secured. In addition to the current charter and ACMI operations, the company has increased its brokering activities, both in terms of arranging for third-party dry and wet leases and aircraft brokering.

12.2.2 BLUEBIRD CARGO

Purpose of the company

Bluebird Cargo is a transportation services provider, operating a fleet of narrow-body freighter aircraft, an air cargo sales agency, and related peripheral services.

History

Founded in the 2000, Bluebird Cargo commenced flight operations in March 2001 with a single Boeing 737-300 freighter aircraft. Services were initially offered on a route from Iceland, via the UK, to Cologne, Germany, in co-operation with the international express parcel company United Parcel Service, UPS. The operation grew steadily by one aircraft per year and by early 2005, Bluebird Cargo was operating five B737-300 freighter aircraft. Bluebird Cargo was acquired by FL Group in 2005.

Management

Þórarinn Kjartansson

The Managing Director of Bluebird Cargo is Þórarinn Kjartansson. Þórarinn has been the Managing Director of Bluebird Cargo since its incorporation in early 2001. He has been involved in the airline business for over two decades working for Loftleiðir and Cargolux in operations, scheduling and marketing and finally as managing director for North America and South America. He was one of the founders of Flugflutningar ehf. (Air Cargo), Bluebird Cargo and Vallarvinir ehf. (Airport Associates, an independent ground handling service company). He received his B.Sc. in economics from the University of Gothenburg in 1978.

Operation

In addition to air freight services to and from Iceland, Bluebird Cargo operates aircraft on a wet-lease basis to three key customers: UPS, TNT, and Alitalia. The wet-lease part of the operation accounts for close to 80% of the total revenue, with the remaining 20% generated by the carriage of general cargo to and from Iceland. The main general cargo clients of Bluebird Cargo are Icelandic freight forwarders, most major international freight forwarders and many large Icelandic exporters. In late November 2006 Blubird Cargo purchased two Boeing 737-400 passenger aircraft which will be transformed to cargo aircraft. These aircraft will be in operation around mid year 2007. It is assumed that one of the company's older aircraft will be sold and the company will therefore operate 6 cargo aircraft at year end 2007.

Market and current market position

Bluebird Cargo has carved out a niche operating short-haul freighter flights in time-sensitive markets within Europe. As such, the company enjoys a fairly favourable market position. The target customer group consists of express service companies, post offices and airlines operating their own overnight networks within Europe. Competition within this segment is mostly limited to other European airlines operating freighter aircraft of similar size and capacity, of which there are not many.

The air cargo sales-agency arm of Bluebird Cargo in Iceland dates back to 1994, providing local sales and marketing representation for airlines such as Cargolux Airlines, UPS Air Cargo, LTU, Luxair and others. Through these companies, Bluebird Cargo gains access to the world-wide air cargo networks of some of the world's leading air freight companies. Bluebird Cargo therefore offers the Icelandic market reliable and fast access to almost any major destination in the world.

Future strategy

Most leading experts agree that the global air freight market will grow rapidly in the coming years. Air freight is projected to grow considerably faster than the passenger side of the industry. The future growth strategy of Bluebird Cargo is based on a two-pronged approach to the market. On the one hand, potential lies in providing aircraft and air freight capacity to the various segments of the air freight industry on a global basis, including wet-lease services to other airlines, contract operations for freight forwarders, and dedicated services to express parcel corporations. On the other, the company will continue to grow with the Icelandic air freight market, building on the strengths outlined above.

12.2.3 ICELEASE AND IG INVEST

Purpose of the company

Icelease is an aircraft trading arrangement company which ties together and utilizes the knowledge, experience and business contacts within Icelandair Group in the business of buying, selling and leasing of aircraft.

History

Icelease was formally founded in early 2005 as a separate business unit specialising in aircraft trading. IG Invest was established in April 2006 as a holding company for Icelease assets.

Management

Kári Kárason

Kári Kárason is the Managing Director of Icelease and IG Invest. Kári was appointed managing director of aircraft trading and leasing on 1 June 2006. He joined FL Group in 1994 and was most recently the CFO of Icelease. He received his Cand.Oecon from the University of Iceland.

Operation

Whenever Icelease arranges an aircraft purchase, a new limited-liability company (special purpose company, SPC) is set up in co-operation with outside investors. Icelease manages a special holding company, IG-Invest, that again holds the shares of the SPC's. The aircraft is then leased to financially sound airlines on a long-term lease agreement that fully covers the aircraft investment company's operations. The SPC's will eventually be sold out of Icelandair Group with the attached leasing contract when market conditions are right, yielding a profit. By attaining long-term lease agreements, the company increases the likelihood of being able to exit when the market cycle is favourable.

Table 8. IG Invest's assets

Operator	**Share**	**Type of aircraft**	**Number of aircraft**
Air China	40%	B737-800	5
Air Baltic	49%	737-500	3
Icelandair	49%	757-200ER	3
Singapore Airlines	49%	B747-400F	1
Upcoming contracts			
Operator	Share	Type of aircraft	Number of aircraft
Hainan Airlines	40%	B737-800	2
Hainan Airlines	100%	B737-801	3
Air Berlin	100%	B737-800	2
Aircraft orders			
Operator	Share	Type of aircraft	Number of aircraft
To be decided	100%	B787-8	4
Aircraft options			
Operator	Share	Type of aircraft	Number of aircraft
To be decided	100%	B787-8	3

Additionally, Icelease arranges back-to-back aircraft trading, where aircraft are sold immediately upon purchase, thereby eliminating the need for the SPC-structure.

The rate of return on aircraft leasing is most sensitive to the purchase price and residual value of an aircraft when it is sold off. Aircraft prices are cyclical due to the fact that supply is mostly fixed while demand changes frequently; also, the residual value of an aircraft is influenced by its age and characteristics, airline preferences and regulations.

Icelease has been involved in 27 aircraft transactions (23 purchases and 4 sales) since its foundation. These deals have so far taken place in Europe and in Asia.

The assets
The current portfolio consists of eleven passenger aircraft, one cargo freighter and 11 future deliveries of passenger aircraft with additional three purchase options. Four of the future deliveries and all three purchase options are B787-8 Dreamliner aircraft, part of which are intended for Icelandair's operation. The options on the Dreamliners are valuable, as the price of these aircraft is currently higher than the price specified in the option agreements, according to the management.

In 2006 and 2007 Boeing is delivering 15 new Boeing 737-800 aircraft. The company has already leased five of them to Air China, seven to Hainan Airlines and placed two with a European carrier. The company reinforced its relationship with Boeing by placing an order for the 737-800 aircraft in the first half of 2005.

Market and current market situation
Aircraft leasing is a large-scale worldwide branch of financial services. During the past 25 years, the number of aircraft owned by leasing companies has been on the rise. Both the world fleet of aircraft and the proportion of the fleet owned by leasing companies have increased in size. Today, about 35% of the world's commercial fleet is owned by leasing companies. Aircraft are critical assets for airlines and they pay about USD 115 billion annually in leases. Many companies have seen opportunities to enter the aircraft leasing business. These companies include General Electric, Daimler Chrysler and Royal Bank of Scotland.

Boeing Market Outlook forecasts the average annual passenger and cargo growth over the next 20 years at 4.8% and 6.2% respectively. Such growth will in turn increase the size of the aircraft market, resulting in improved liquidity of assets.

Future strategy
Icelease is aware that the success of its operations is highly dependent on the market cycle. The company intends to utilize the market cycle to maximize its return on equity. The company seeks long-term leasing contracts on its aircraft, preferably 5-10 year contracts, except in cases when the market is very weak. Having a long-term contract on the aircraft increases the odds that the market will peak while the asset is under contract. In order to be able to sell an asset with an attached leasing contract in a peak market, the company needs to discount it to make up for the difference between current market leasing rates and the contract lease rate. It is difficult to time the market peak, and therefore the company reduces its overall risk by entering into long-term contracts instead of running the risk of a contract expiring when the market is at a low and no lessee can be found.

The company will actively search for equity partners in its aircraft investments. The company ideally wishes to have less than a 50% stake in each investment.

12.3 TRAVEL & TOURISM INFRASTRUCTURE

Three companies (Iceland Travel, a tour operator and travel agency in in-coming tourism, Icelandair Hotels, which markets and operates two hotel chains, Icelandair Hotels and Edda Hotels, and Air Iceland a scheduled domestic carrier which also offers regular flights to Greenland and the Faeroe Islands) form the travel and tourism part of the Group.

Even though these companies all provide strategic support to the international scheduled operations, their main focus is on profitable operations. All these companies have recently seen an improvement in results and are now able to profitably harvest the growth in tourists coming to Iceland.

12.3.1 AIR ICELAND (FLUGFÉLAG ÍSLANDS)

Purpose of the company
Air Iceland is a market-driven service company responsible for seven scheduled domestic flights as well as routes from Iceland to the Faroe Islands and Greenland.

History
Air Iceland was formed in 1997 when Icelandair Domestic was merged with Flugfélag Norðurlands, but the airline traces its roots back to 1937.

Management
Árni Gunnarsson
The Managing Director of Air Iceland is Árni Gunnarsson. Árni was appointed to his current position in March 2005. He previously worked as Director of Sales and Marketing at Air Iceland, Managing Director at Ferðaskrifstofa Íslands / ITB, Managing Director of Iceland Travel and as Director of Icelandair Holidays. He worked for the German Tour Operator FTI in Münich as director of Risk Management in 1993-1997. Árni is MSc. in Economics from Augsburg University, Germany.

Operation
The company operates flights on seven domestic routes and two international routes, and on one additional international route over the summer. About 90% of its passenger traffic is on the routes between Reykjavík, Akureyri, Ísafjörður and Egilsstaðir. In 2005, flight operations were extended to the Faroe Islands in co-operation with Atlantic Airways, and to Greenland. Air Iceland has entered into a five year agreement with Greenland's local authorities on flights between Reykjavík and Kulusuk and Constable Point. In 2004 the company acquired three Fokker 50 aircraft and currently has six such aircraft in operation. The company purchased two DASH 8-100 aircraft which started operation this year. In addition the company operates smaller aircraft, namely Twin Otter.

Market and current market position
Air Iceland holds a strong position on the Icelandic domestic air transport market[6] and has operated profitably over the past three years. With the strong economy and large-scale industrial projects in progress in Eastern Iceland, demand has been high on main routes and is expected to remain high. The busiest routes are to Ísafjörður, Egilsstaðir and Akureyri; despite the industrial activity in Eastern-Iceland, the frequency of flights to Akureyri has increased more than to Egilsstaðir since operations went underway in the eastern part of Iceland. Air Iceland also operates flights to Greenland and the Faroe Islands.

Future strategy
Air Iceland plans to grow and increase profitability by offering the Icelandic market and the tourism market in Iceland the best possible service. Demand is good and growing on all destinations within Iceland and to Greenland, which is the most promising external market. Air Iceland aims to become a West Nordic airline.

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6 In 2005 the total number of passengers on domestic flights was 411,639 according to information from the Icelandic Civil Aviation Administration available via the website http://www.caa.is/media/files/flugt_isl_2005.pdf. In 2005 Air Iceland transferred around 321,001 passengers on domestic routes.

SUMMARY

SECURITIES NOTE

REGISTRATION DOCUMENT

12.3.2 ICELANDAIR HOTELS

Purpose of the company

Icelandair Hotels aims to market and operate profitably two hotel chains: All-year hotels under the trademark Icelandair Hotels, and summer hotels under the trademark Edda Hotels.

History

The airline Loftleiðir started to operate a small hotel at Keflavik Airport in 1962 and built Hotel Loftleiðir in 1966 in Reykjavik. After being a part of the airline's general operations for over 30 years, the hotel arm was turned into a separate and distinct subsidiary in 1998.

Management

Magnea Þórey Hjálmarsdóttir

The Managing Director of Icelandair Hotels is Magnea Þórey Hjálmarsdóttir. Magnea was appointed in July 2005 but joined Icelandair Hotels in 1994. Magnea has worked in the hotel industry since 1991 and held management positions within hotels in Iceland, Switzerland and Japan. She received her MBA from the University of Surrey UK in 2003

Operation

Icelandair hotels run eight Icelandair hotels and 15 Edda hotels. All the hotels, apart from five outside Reykjavik, are operated by Icelandair Hotels. They are run according to a franchise agreement which allows them to use the trademark Icelandair Hotels. Icelandair Hotels are: Nordica Hotel, Hotel Loftleiðir, Flughótel, Hotel Flúðir, Hotel Rangá, Hotel Kirkjubæjarklaustur, Hotel Hérað and Hotel Hamar. The Hotel Edda chain has a total of 15 hotels around the country which are open during the summer. Most of them use the student quarters of schools, with the number of guestrooms ranging from 20–204 and of differing quality. Icelandair Hotels rents all real estate that it uses for its operations.

Market and current market position

The number of tourists in Iceland has grown rapidly[7], and Icelandair Hotels has more than doubled its capacity in the last five years. The two hotels in Reykjavik account for approximately 75% of Icelandair Hotels' revenue: Hotel Lofteiðir, a four-star hotel with 220 rooms and the recently-renovated Nordica Hotel, a four-star 252-room hotel with convention facilities. The main competitors of Icelandair Hotels are more centrally located 3 and 4 star hotels in Reykjavik; the main competitors of the Edda hotels are the Foss Hotel chain and Icelandic Farm Holidays. The market has expanded, due both to the growth in tourism in recent years and also increased capacity.

Future strategy

With clear focus on cost and aggressive marketing, Icelandair Hotels expects to return to profitability this year and grow over the next few years. It is looking closely at developments in Reykjavik with the intention of being an active partner in hotel operations in the city centre.

[7] Figures for number of tourist visiting Iceland can be found via the website http://www.ferdamalastofa.is/displayer.asp?cat_id=503

12.3.3 ICELAND TRAVEL

Purpose of the company

Iceland Travel is a tour operator and travel agency in incoming tourism, conferences and incentives in Iceland. Its main goal is to offer a wide range of services in order to meet the needs of its customers.

History

For over 30 years, the company has grown and prospered; in 2005, over 35,000 visitors travelled to Iceland with Iceland Travel. The company's turnover has increased each year and was just under ISK 2 billion in 2005. Iceland Travel is a member of the Icelandic Travel Industry Association, SAF (The Icelandic Travel Industry Association) and the Iceland Convention and Incentive Bureau, IC&IB. In addition, Iceland Travel is a member of "Destinations Unlimited" and "Prestige Resorts and Destinations", associations operating on the convention and incentive market.

Management

Jóhann Kristjánsson

The Managing Director of Iceland Travel is Jóhann Kristjánsson. Jóhann was appointed in January 2006 after over 10 years as a manager in the information technology business at Skyrr and Glitnir banki hf.. Previously he had obtained some hands-on experience within the travel industry from Denmark. He received his Cand.Oecon from the University of Iceland in 1992 and an MBA degree from Copenhagen Business School (CBS) in 1997.

Operation

Iceland Travel operation is producing, marketing, distributing and selling package tours to foreign tourists in Iceland. It specializes in advanced services and working with almost all licensed vendors operating in the tourist industry in Iceland - from car rentals to hotels and accommodation providers, professional guides, etc. Iceland Travel's well-educated, experienced and creative team is the key to its high standards of service and successful operation. The aim is to offer high quality service at competitive prices at all times.

Market and current market position

Iceland Travel is providing travel and MICE services in Iceland. The focus is on profitable packages and increasing focus on internet sales channels. About 75% of Iceland Travel's customers are contracted customers, foreign travel wholesalers and Icelandic companies and institutions.

Future strategy

In January 2006, a new managing director, Jóhann Kristjánsson, was engaged at Iceland Travel and his new management will focus its attention on using the Internet as a sale channel more effectively and highlighting products that have the highest margin, high-end conference and incentive markets and new markets such as the Far East (China). Iceland still has a great deal of potential as a destination for tourists, conferences and incentives, as the infrastructure is improving. New hotels, routes, places and activities are being brought to the market and the knowledge needed to provide a professional service to the market is developing. Iceland Travel’s mission is to lead that market growth.

12.4 OTHER SUBSIDIARIES

12.4.1 ICELANDAIR SHARED SERVICES

Purpose of the company

Icelandair Shared Services handles the accounting, reporting and salary processing for the companies within Icelandair Group.

History

Icelandair Shared Services was established in 2002 with the merger of FL Group's and its subsidiaries' accounting departments.

Management

Magnús Kr. Ingason

The Managing Director of Icelandair Shared Services is Magnús Kr. Ingason. Magnús has been the General Manager of the company Shared Services since its incorporation in the year end 2002. He joined Flugleiðir in 1998 and was previously Director of Flugleiðir's accounting department. Magnús received his Cand.Oceon from the University of Iceland in 1993 and became a certified public accountant in 1999.

Operation

When it was established, the company was one of the largest companies in Iceland specializing in this area of business and is intended to operate a support department for finances with the shared services concept as a cornerstone. This service involves accounting, collection, payments, payroll, tax reporting and preparation of financial statements, in addition to other specialised services for managers of the group. Icelandair Shared Services is a frontrunner in Iceland in its field of operation and its 80 employees possess extensive knowledge of this area of business.

Future strategy

Icelandair Shared Services aims to continue process-smoothing and simplification with unit-cost reduction as a main target and to push forward timelines for publication of financial data, both internal and external, in order to increase the value of financial information within the group.

12.4.2 ICECAP

Purpose of the company

Icecap underwrites a part of Icelandair Group's insurance risk.

History

Icelandair formed a captive insurance company in Guernsey in 1996. The company rented access to a so called "Protective Cell" with Harlequin, a local insurance company. Through the years the equity of the company increased and 2004 it was decided to form Icelandair's own Protective Cell company around this operation.

Management

The management of the operation of IceCap is included in the Icelandair Group management.

Operation

Instead of insuring with a typical insurance company, a similar premium is paid to Icelandair Group's own company which then underwrites part of the risk and reinsures the remaining risk out to the market.

Future strategy

Icecap plans to underwrite more of Icelandair Group's insurance risk as well as minimise the reinsurance that the company buys from the market.

13 OPERATING ASSETS

Table 9. The Company's property, plant and equipment as of September 30, 2006. All figures in ISK millions.

	Aircraft and flight equipment	Engines	Aircraft and engines	Buildings	Other	Total
Cost						
Balance at 1 January 2006	17.053	920	17.973	2.204	2.664	22.841
Exchange rate difference	1.189	76	1.265	0	(0)	1.265
Additions through business combinations	8	0	8	0	10	18
Additions during the year	2.699	944	3.644	0	232	3.875
Sales and disposals during the period	(1.551)	0	(1.551)	0	(57)	(1.608)
Balance at 30 September 2006	19.398	1.940	21.338	2.204	2.849	26.391
Depreciation and impairment losses						
Balance at 1 January 2006	1.024	0	1.024	61	1.160	2.245
Exchange rate diference	1	0	1	0	0	1
Depreciation	921	314	1.235	80	250	1.565
Sales and disposals during the period	(52)	0	(52)	0	(52)	(104)
Balance at 30 September 2006	1.894	314	2.208	141	1.358	3.707
Net						
1.1.2006	16.029	920	16.949	2.143	1.504	20.596
30.9.2006	17.504	1.626	19.130	2.063	1.491	22.684
Depreciation ratio	4-10%	4-10%		2-4%	12-33%	

13.1 BUILDINGS

On September 30, 2006 the book value of total real estate property of Icelandair Group amounted to ISK 2,063 million and total lease obligations amounted to ISK 5,344 million. The most significant buildings are listed in Table 10 below.

Table 10. Icelandair Group's material real estate property. All figures in ISK million.

	book value
Hótel Nordica, Suðurlandsbraut 2, Reykjavík	Leased
Hotel Loftleidir, Reykjavik airport, Reykjavík	Leased
Hotel Herad, Midvangi 5-7, Egilsstadir	Leased
Icelandair Sales office, Baltimore, USA	Leased
Icelandair Sales office, London, UK	Leased
Icelandair Sales office, Copenhagen, Denmark	Leased
Maintenance Hangar at Keflavik airport	669
Freightcenter at Keflavík airport	340
Officebuilding at Reykjavík airport	320
Servicebuilding at Keflavík airport	267
Hangar 4 and other buildings at Reykavik airport	340
Skútuvogur 13A, Reykjavík	118

13.2 AIRCRAFT AND FLIGHT EQUIPMENT

The total fleet connected to Icelandair Group's subsidiaries is listed in Table 11., including the 19[8] aircraft managed by Icelease, some of which have not yet been delivered. The ownership of aircraft related to Icelease is explained in section 12.2.3. For other subsidiaries owned aircraft are:

- Five Boeing 757 – 200 operated by Icelandair
- Two Boeing 757 – 200 operated by Icelandair Cargo
- Two Boeing 737 – 400 operated by Bluebird Cargo
- Ten aircraft operated by Air Iceland

On 30 September 2006 the combined value of all owned aircraft and flight equipment amount to ISK 19,130 million. Total lease obligations relating to aircraft and flight equipment came to ISK 15,112 million.

As a part of Latcharter's expansion plans, the company has, since 30 September 2006, added two leased Airbus A320 aircraft to it's fleet. These aircraft will be used to fulfill a three years contract with Israir Airlines of Israel. Latcharter is currently negotiating contracts with customers for up to 4 additional Airbus A320 aircraft, that it can lease from the same source. Additionally, Latcharter has bought and sold one of the Airbus A320 aircraft it had previously operated. Hence, this aircraft will leave the fleet during the month of February.

Icelandair has signed letters of intent for the lease of three Boeing 757-200ER aircraft, which will be used for the expanded scheduled network during Summer 07, and to replace an older Boeing 757 which will be returned to it's owner. Additionally, a Boeing 767-300ER will be subleased through Loftleidir Icelandic to a South American airline for the next three years.

Table 11. Total fleet connected to Icelandair Group on 31 December 2006.

	Icelandair	Icelandair Cargo	Loftleiðir Icelandic	Bluebird Cargo	Icelease	Air Iceland
5 Boeing 737-300				5		
21 Boeing 757-200	9	5	4		3	
3 Boeing 767-300	1		2			
1 Boeing 747-300					1	
1 Boeing 757-300	1					
6 Fokker Friendship, 2 Twinotter, 2 Dash						10
2 Airbus 320-200			2			
2 Boeing 737-400				2		
3 Boeing 737-500					3	
12 Boeing 737-800					12	
	11	**5**	**8**	**7**	**19**	**10**

[8] In addition to the 19 aircraft, Icelease has made a binding agreement to purchase four Boeing 787-8 Dreamliner aircraft

13.3 OTHER PROPERTY AND EQUIPMENT

The combined value of all owned property and equipment outside buildings and aircraft and flight equipment is ISK 1,491 million and ISK 228 million for leased property. The most significant tangible assets other than buildings and aircraft and flight equipment are listed in Table 12.

Table 12. The most significant other property and equipment

	Book value
Interiors at Nordica Hotel	646
Interiors at Loftleidir Hotel	59
Interiors at Officebuilding at Reykjavik airport	146
Interiors at Keflavik airport	111
Airport equipment at Keflavík airport	119
Artwork and paintings	100

SUMMARY SECURITIES NOTE REGISTRATION DOCUMENT

14 INVESTMENTS

Table 13. Investments in each of the years 2003-2005 and year to date 2006, total amount invested and percentage of the total capital expenditure for the year.

Year	Investment	ISK millions	% of capex
2006	2 Boeing 737-400	2,200	39%
2006	Latcharter Airlines	507	9%
2006	2 Dash 8-100 aircraft	685	12%
2006	Boeing 757-200 winglets	280	5%
2006	Airline Services Estonia	104	2%
2006	Other	1,850	33%
2005	2 engines	400	20%
2005	Hotel Nordica	300	15%
2005	ITS spare parts	250	13%
2005	Other	1,244	63%
2004	3 F-50 aircraft	400	22%
2004	ITS spare parts	250	14%
2004	Hotel Nordica	120	7%
2004	Other	1,015	57%
2003	Hotel Nordica	600	25%
2003	ITS	600	25%
2003	Other	1,179	50%

14.1 HISTORICAL INVESTMENTS

All investments of Icelandair Group for the period 2003-2005 were financed internally. Investments are mainly due to investment in aircraft, flight equipment and aircraft engines. Aircraft engines and aircraft spare parts are stated at cost less accumulated depreciation and impairment losses. When aircraft are acquired the purchase price is divided between the aircraft itself and engine hours. Aircraft are depreciated over the estimated useful life of the relevant aircraft until a residual value is met. Engine hours 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 there is any, is expensed in full.

In 2003 total investment in property plant and equipment came to ISK 2,379 millions. The Company's principal investments that year were mainly due to Hotel Nordica for ISK 600 million and ITS for ISK 600 million. Air Iceland bought one Metro23 aircraft and two Twin Otter aircraft for ISK 400 million.

In 2004, total investments amounted to ISK 1,785 millions. Air Iceland bought 3 F-50 aircraft for ISK 400 million and ITS bought spare parts for ISK 250 million and invested ISK 120 million in Hotel Nordica.

In 2005 total investments was ISK 2,194 with material investment consisting of 2 engines for ISK 400 million and an ISK 300 million investment in Hotel Nordica. ITS purchased spare parts for ISK 250 million.

14.2 CURRENT INVESTMENTS

Investments in 2006 are estimated at ISK 5,626 million which is unusually high due to exceptional items. All investments except the purchase of two Boeing 737-400 aircraft are financed internally. Icelandair Group acquired the majority of the shares in the Latvian charter operator LatCharter Airlines for ISK 507 million and committed itself to acquire the remaining shares in the future. The Company also purchased two used, but completely overhauled, DASH 8-100 aircraft from the Canadian aircraft producer Bombardier, representing a total investment of ISK 685 million. The aircraft are to be used mainly in relation to contracts that Air Iceland has with the government in Greenland but also on domestic routes. Other material investments this year include ISK 280 million for winglets for Boeing 757-200 aircraft and ISK 104 million in Airlines Services Estonia (ASE) which is based in Tallinn, Estonia. ASE is a specialist in airline revenue accounting.

14.2.1 TWO BOEING 737 – 400 AIRCRAFT

The two Boeing 737-400 aircraft were purchased to renew the fleet of Bluebird Cargo and to exchange two of the Boeing 737-300 aircraft of the company. The plan is to sell the Boeing 737-300, but it will probably not be finalised before year end 2006. The sales price of the Boeing 737-300 is estimated USD 12 million per aircraft. The new Boeing 737-400 have 35% more carrying capacity which opens up the opportunity of longer and more efficient contracts with suppliers, than their predecessors. In addition, they are relatively more practical in operation which will improve Bluebird Cargo's performance.

14.2.2 LATCHARTER AIRLINES

Loftleiðir-Icelandic, the charter and ACMI-marketing subsidiary of the Icelandair Group, bought 55% of the shares in LatCharter in June 2006 and has signed an obligation to buy the remaining 45%. The price of the remaining shares is dependant on the EBITDA results of LatCharter for the years 2006, 2007 and 2008. A minimum and a maximum price has been set in the contract, the minimum being EUR 4.5 million and maximum EUR 13.5 million. The purchase price of the 55% of the shares has been accounted for in Loftleiðir's books, as has also the minimum price of the remaining shares, EUR 4.5 million, which is still unpaid. The final purchase price will be set after the audited accounts for 2008 are available.

The acquisition comes as a result of the ongoing co-operation between the two companies announced earlier this year and is part of Loftleiðir-Icelandic's strategy to strengthen its position in the Baltic and CIS region and to add the Airbus family into its world-wide ACMI product line.

LatCharter Airlines has built up a solid and positive reputation in the Baltic region and has close relations with the local charter market. Furthermore, the company has gained extensive knowledge of the CIS market, which will undoubtedly be of benefit to Lofleidir Icelandic in the near future, opening the window for its current product line.

LatCharter Airlines was established in Latvia in 1992. The company started its operations with several Soviet-built aircraft, but gradually changed its fleet to two modern Airbus-A320s. By 2006 the company had grown substantially, both in terms of the number of passengers carried and of the number of destinations served, and it has become the leading provider of charter flights in Latvia. Meanwhile, the company has also started to offer wet-lease services outside Latvia. In 2005, the company carried 100,000 passengers and its turnover reached EUR 17 million (up from EUR 13 million in 2004). Currently LatCharter Airlines employs 87 people.

14.2.3 AIRLINE SERVICES ESTONIA (ASE)

Icelandair Shared Services, one of the Icelandair Group companies, has bought Airline Services Estonia (ASE) which is based in Tallinn, Estonia. ASE is a specialist in airline revenue accounting.

The company will, on behalf of Icelandair Shared Services, be responsible for the sales and revenue accounting for Icelandair and this merger creates further opportunities for this area.

The operation of ASE, which specialises in sales and revenue accounting for airlines, is an important part of the services that Icelandair Shared Services offer. This purchase will increase the operational efficiencies and lower costs by moving this part of the operations to Estonia. There will also be many opportunities for increased business in this area. ASE is already providing revenue accounting for other airlines, and there are opportunities to increase the revenue.

Icelandair Shared Services currently employs 83 persons and ASE about 40.

14.3 FUTURE INVESTMENT

The company has made binding agreements to invest in new seats and an in flight entertainment system for Icelandair Boeing 757 aircraft for a total of USD 10 million in 2007 and USD 20 million in 2008. The Company envisages financing these investments by internally generated funds.

The company has signed a letter of intent regarding the purchase of two Boeing 757-200 passenger aircraft. These aircraft are currently leased by Loftleiðir-Icelandic and Icelandair.

Icelandair has ordered and confirmed four Boeing 787 aircraft – Dreamliners – for delivery in 2010-12. The airline has also confirmed options for 3 more such aircraft, for possible delivery in 2012-2013. The management of the Company has not decided on method of financing the aircraft.

No other material investments in tangible fixed assets are planned.

15 BOARD OF DIRECTORS AND MANAGEMENT

15.1 BOARD OF DIRECTORS

The board of directors of the Company has supreme authority in the Company's general affairs between shareholders meetings and endeavours to keep its organization and operations on course. The Company's board of directors directs company affairs and sets its objective and future vision, dealing with the annual budgets and company's goals presented by the CEO and the strategy to be taken to reach them. The board of directors is expected to ensure that the Company's strategy is in accordance with its vision and overall goals. The Company's board of directors ensures the sufficient supervision of the accounting and handling of the Company's funds.

The board of directors takes decisions on all matters that are deemed extraordinary or significant. The board of directors may grant the CEO the authority to resolve such issues. The CEO may also execute such matters if there is no opportunity to wait for the board of directors' approval without this resulting in great disadvantage to the operations of the Company. In such instances, the CEO is to report promptly to the chairman of the board of directors. Only the Company's board of directors can grant power of procuration.

The board of directors appoints the Company's CEO and decides on the terms of his or her employment or entrusts the chairman of the board of directors with this task.

The working procedures of the board of directors state that board members are to familiarise themselves with the provisions of law, the Company's Articles of Association, general securities regulations and regulations on the handling of inside information and insider trading.

The following section lists the current members of the board of directors and their activities for the past five years.

FINNUR INGÓLFSSON, Jöklafold 15, 112 Reykjavík, Iceland

Chairman of the board of directors since October 2006

Finnur Ingólfsson was the CEO of VÍS - the Icelandic Insurance Company from 2002 until May 2006. In the years 2000-2002 Finnur was the Director of the Central Bank of Iceland and in the years 1995-1999, Finnur was Iceland's Minister of Industry and Commerce. He was a member of Parliament, Reykjavík constituency, for the Progressive Party in Iceland. Finnur was a Special Assistant to the Minister of Health and Social Security in the years 1987-1991 and a Special Assistant to the Minister of Fisheries in the years 1983-1987. He was a teacher of economy at the Flensborg Secondary School in Hafnarfjörður in the years 1977-1978 and the Managing Director of the Dyngja Knitting Co. in the years 1977-1978 and of Katla Knitting Co. in the years 1975-1976. Finnur holds a BS degree in Business from the University of Iceland.

Current board positions:

Current member of the board of directors of Icelandair Group hf., Langflug ehf., Kaupþing banki hf., Íshestar ehf., Bolmagn ehf., FISK-eignarhaldsfélag ehf., Íslensk endurtrygging ehf., Hvanná ehf., Fikt ehf. and Foldás ehf.

Past board positions:

Icelandair Group Holding hf., Lýsing hf., Vátryggingarfélag Íslands hf., Öryggismiðstöð Íslands hf., VÍS International Invest ehf., Íslenskar endurtryggingar hf., Líftryggingarfélag Íslands hf. and Flutningar ehf.

Other information:

CEO of Vátryggingarfélag Íslands from 2002-2006, CEO of Líftryggingarfélag Íslands from 2005-2006 and member of the board of governors of the Central Bank of Iceland from 2000-2002.

Own holding of shares: None

Holdings of financially related parties: Finnur is member of the board of directors of Langflug ehf. and owner of 25.0% of Langflug ehf.'s share capital the other 75.0% is owned by Eignarhaldsfélagið Samvinnutryggingar svf.. Langflug ehf. owns 320 million shares or 32.0% of the total share capital of Icelandair Group hf.

Call or put options: None

ÓMAR BENEDIKTSSON, Ægissíða 58, 107 Reykjavík, Iceland
Vice-chairman of the board of directors since October 2006
Ómar Benediktsson was the CEO of Islandsflug from 1997 until 2004 when the company merged with Air Atlanta Icelandic and became the CEO of the joint company. After the merger was complete he left the company at the end of 2005. He was the MD of Island Tours in Germany 1986-1992. After that he was involved in several companies as an investor and a board member. Ómar was one of the founders of Icelandair Group Holding hf. on its date of establishment on 15 October 2006. Ómar has a degree in Business Administration from the University of Iceland.

Current board positions:
Current member of the board of directors of Icelandair Group hf., Penninn hf., Flugfjarskipti ehf. and Eignarhaldsfélagið City Star Airlines hf.

Past board positions:
Icelandair Group Holding hf., Íslandsflug hf., Flugfélagið Air Atlanta hf., Avion Aricraft Trading hf. and Suðurflug hf.

Other information:
Former CEO of Íslandsflug hf. (later named Air Atlanta Icelandic hf.)

Own holding of shares: None

Holdings of financially related parties:
Majority owner of Blue Sky Transport Holding SA which owns 66.7% in Urður ehf. Urður ehf. holds 55,555,556 shares in Icelandair Group hf. or 5.6% of the total share capital.

Call or put options: None

HERMANN S. GUÐMUNDSSON, Suðurlandsbraut 18, 108 Reykjavík, Iceland
Member of the board of directors since October 2006
Hermann Guðmundsson was appointed CEO of Olíufélagið hf. and BNT hf. in 2006 after being the CEO of Bílanaust hf., BNT hf.'s subsidiary, from the year 2002. In the years 1994-2002, Hermann worked as a sales represententative and later the CEO of Slípivörur og verkfæri ehf. Hermann studied Development and Leadership at the IESE business school in Barcelona in the year 2005, and AMP studies from the Business School in Barcelona in the years 2004-2005. In the years 1978-1984, Hermann studied at Iceland's Hotel and Catering Academy.

Current board positions:
Current member of the board of directors of Icelandair Group hf., Naust ehf., Drang-hlutur ehf., Tunguós ehf., Hjólbarðahöllin ehf., Ísdekk ehf., Fjárfestingarsjóður Stórkaupmanna (an investment fund), AT Toolcentre Ltd. and Bílanaust hf.

Past board positions:
Icelandair Group Holding hf., Strax-fast ehf. and Slípivörur og verkfæri ehf.

Other information:
Hermann is the current CEO of Olíufélagið hf. and BNT hf. and former CEO of Bílanaust hf. and Slípivörur og verkfæri hf.

Own holding of shares: None

Holdings of financially related parties:
CEO and owner of 1.3% of the share capital in BNT hf., which owns 49.9% share in Naust ehf. Naust ehf. holds 148,148,148 shares in Icelandair Group hf. or 14.8% of the total share capital.

Call or put options: None

JÓHANN MAGNÚSSON, Suðurlandsbraut 18, 108 Reykjavík, Iceland
Member of the board of directors since November 2006
Jóhann Magnússon was Managing Director of FBA Corporate Advisory Ltd. and subsequently ISB (Íslandsbanki now Glitnir banki hf.) Corporate Advisory from 1999 until 2002. Previously, Jóhann was Managing Director of Ker ehf., which was then a subsidiary of Olíufélagið hf. A Management Consultant at Stuðull ehf. for 14 years, Jóhann was one of its two founders and owners. Prior to that, he was a Management Consultant at Hagvangur hf. for 1 year and Marketing Manager at Vífilfell hf. (Coca Cola - Iceland) for 4 years. Currently Jóhann is the CEO of Carta Capital. He holds a Cand.Oecon. degree from the University of Iceland.

Current board positions:
Current member of the board of directors of Carta Capital ehf., Carta Capital LTD. UK, J.K.B. ehf., Investor ehf. and Aptom Holdings Limited, Jersey.

Past board positions:
Icelandair Group Holding hf., Basisbank A/S and Smartkort hf.

Other information:
CEO of J.K.B ehf.

Own holding of shares: None
Holdings of financially related parties: None
Call or put options: None

MARTA EIRÍKSDÓTTIR, Vesturbrún 33, 104 Reykjavík, Iceland
Member of the board of directors since November 2006
Marta Eiríksdóttir is currently Head of Marketing and Business Relations for Landsnet which is the Transmission Service Operator of electricity in Iceland. Prior to that Marta was Executive Director of Marketing of Consumer Products at Íslandssími. During 1994-2000 Marta Eiríksdóttir worked as Manager Commercial Programmes for Europay International, European headquarters of MasterCard, Maestro and eurocheque. Before joining Europay Int. she worked for five years as Head of the Marketing at Eurocard Iceland. Marta has also worked as a consultant on several projects in the credit card industry. Marta holds a degree in Economics and Business Administration from the University of Iceland. She also holds a B.Ed. degree from the University College of Education in Iceland.

Current board positions:
Current member of the board of directors of Netorka hf. and Lítill heimur ehf. and alternate member of the board of directors of Kaupþing Banki hf.

Past board positions:
Icelandair Group Holding hf., Visa Ísland, EJS (chairman of the board from October 2005 to March 2006) and EFIL (European Federation for Intercultural Learning).

Other information:
Head of Marketing and Business Relations of Landsnet ehf.

Own holding of shares: 92.592 shares.
Holdings of financially related parties: None
Call or put options: None

EINAR SVEINSSON, Bakkaflöt 10, 210 Garðabær, Iceland
Member of the board of directors since November 2006
Einar Sveinsson graduated from Menntaskólinn í Reykjavík in 1968. Einar is the former CEO of the Sjóvá-Almennar insurance company. He was employed at Sjóvátryggingarfélag Íslands hf. from 1972 to 2004 (Sjóvá-Almennar tryggingar hf. from 1989), as Chief Executive Officer from 1984 to 2004. Einar is the chairman of the board of Glitnir banki hf. He was chairman of the Iceland Chamber of Commerce from 1992 to 1996. Among other things, he has been chairman of the board of the life insurance company Sameinaða líftryggingafélagið hf., fisheries company Haraldur Böðvarsson hf., Frumherji hf., NAIG (Nordic aviation insurance group), and the Association of Icelandic Insurance Companies. He has also served on the board of directors of the fisheries companies Grandi hf. and Útgerðarfélag Akureyringa hf., and the financing company Lýsing hf.

Current board positions:
Current chairman of the board of directors of Glitnir banki hf., Íslensk endurtrygging hf., Birnir sf., Hrómundur ehf., Áning fjarfestingarfélag ehf. and Gildruklettar ehf. and member of the board of Sjóvá-Almennar tryggingar hf., BNT hf., BNB ehf. and Olíufélagið ehf.

Past board positions:
Icelandair Group Holding hf. and Hf. Eimskipafélag Íslands in 2003.

Other information:
Former CEO of Sjóvá-Almennar tryggingar hf.

Own holding of shares: None

Holdings of financially related parties:
Owner of 7.0% of the share capital in BNT hf., which owns 49.9% share in Naust ehf. and the owner of Hrómundur ehf. which holds 10% of the share capital in BNT hf. The chairman of the board of directors of BNT hf. is Bjarni Benediktsson, who is the son of Benedikt Sveinsson. Benedikt is the brother of Einar Sveinsson. Benedikt Sveinsson is the owner of Hafsilfur ehf., which owns 10% of the share capital in Naust ehf. Furthermore, Einar Sveinsson is the chairman of the board of directors of Glitnir banki hf. which is the owner of 30.1% of the share capital in Naust ehf. Glitnir banki hf.'s shareholdings are explained in section 18.1.

Naust ehf. holds 148,148,148 shares in Icelandair Group hf. or 14.8% of the total share capital.

Call or put options: None

HELGI SIGURÐUR GUÐMUNDSSON, Barónsstíg 47, 101 Reykjavík, Iceland

Member of the board of directors since November 2006

Helgi Sigurður Guðmundsson was appointed the director of operations at the Primary Health Care of the Capital Area in the year 1999. In the years 1989-1998 he was the director of sales at Iceland Insurance Company Ltd. and a sales manager at Samvinn Mutual Insurance in the years 1982-1989. Helgi holds a degree from the Icelandic Management Academy, where he took a program in marketing and insurance management.

Current board positions:

Chairman of the board of directors of the Central Bank of Iceland and member of the board of directors of Foldás ehf.

Past board positions:

Icelandair Group Holding hf., Reykjavík Health Clinic, Landsbanki Íslands hf., Lífeyrissjóður Bankamanna (pension fund), Síminn hf. and the Central Bank of Iceland.

Own holding of shares: None

Holdings of financially related parties: None

Call or put options: None

15.2 SENIOR MANAGEMENT

The senior management team, under the leadership of the CEO, Jón Karl Ólafsson, comprises three managing directors, as is described in Section 12. Senior managers are persons who are relevant to establishing that the Company has the appropriate expertise and experience for the management of its business. The following section lists the current Senior Managers and their activities over the last five years.

JÓN KARL ÓLAFSSON, Reykjavík Airport, 101 Reykjavík, Iceland

CEO of Icelandair Group hf. and Icelandair ehf.

Jón Karl was appointed chief executive officer of Icelandair on 1 June 2005 and became the CEO of Icelandair Group in October 2005. He joined Flugleiðir in 1984, first in the finance department, then as the manager of Flugleiðir's route network. He then served as the general manager of Flugleiðir's office in Frankfurt, Germany, for 5 years. Before being appointed the CEO of Icelandair he had been managing director of Air Iceland since 1999. He received his Cand.Oecon from the University of Iceland in 1984.

Current board positions:

Íslenska óperan, Útflutningsráð (Trade Council of Iceland), Golf ehf., Flugval ehf., and various board positions of current subsidiaries of Icelandair Group.

Past board positions:

None other than subsidiaries of Icelandair Group.

Own holding of shares: 103,703 shares

Holdings of financially related parties:

Jón Karl is the owner of Flugval ehf., Icelandic ID No. 511006-0230. Flugval ehf. owns 18,518,519 shares or 1.9% of the total share capital of Icelandair Group hf.

Call or put options: Call options for a total of 5,000,000 shares at the price of 27.5 per share. One third of the total amount can be purchased for four weeks from 3 January for each of the years 2008, 2009 and 2010.

HLYNUR ELÍSSON, Reykjavík Airport, 101 Reykjavík, Iceland
CFO Icelandair Group hf.

Hlynur was appointed Chief Financial Officer of Icelandair Group in 2006 after being Icelandair's Senior Vice President of Finance and Resource Management since 1 April 2005. He joined Flugleiðir in 1995 as Director of Finance of the domestic airline operation and of Air Iceland from 1997. He holds a BS degree in Business from Rockford College, Illinois since 1991.

Board positions:
Hlynur holds, and has in the past five years held, various board positions within Icelandair Group's subsidiaries. He is also a member of the board of EFIA (the Icelandic Pilots' Pension Fund).

Own holding of shares: 103,703 shares

Holdings of financially related parties:
Hlynur is the owner of Flugfar ehf., Icelandic ID No. 631006-3450. Flugfar ehf. owns 2,222,223 shares or 0,2% of the total share capital of Icelandair Group hf.

Call or put options: Call options for a total of 2,900,000 shares at the price of 27.5 per share. One third of the total amount can be purchased for four weeks from 3 January for each of the years 2008, 2009 and 2010.

SIGÞÓR EINARSSON, Reykjavík Airport, 101 Reykjavík, Iceland
COO Icelandair Group hf.

Sigþór was appointed COO of Icelandair Group in March 2006. He was managing director of Loftleiðir-Icelandic from its foundation on January 1, 2002 until 2006. He joined Flugleiðir in April 1996, first in positions related to strategic planning, but as of May 1999 he served as Director of Resource Management where he assumed responsibility for management of all flight-related costs, including aircraft leasing, station management and fuel purchasing. He holds a master's degree in industrial engineering and management.

Board positions:
Sigþór holds, and has in the past five years held, various board positions within Icelandair Group's subsidiaries.

Own holding of shares: 103,703 shares

Holdings of financially related parties:
Sigþór is the owner of Fjárfestingafélag Tannanes ehf., Icelandic ID No. 631006-2050. Fjárfestingafélag Tannanes ehf. owns 3,703,704 shares or 0,4% of the total share capital of Icelandair Group hf.

Call or put options: Call options for a total of 2,900,000 shares at the price of 27.5 per share. One third of the total amount can be purchased for four weeks from 3 January for each of the years 2008, 2009 and 2010.

15.3 CONFLICT OF INTEREST

BNT hf. is the majority owner of Olíufélagið ehf., which is the Company's main fuel supplier. Therefore, attention is drawn to Hermann S. Guðmundsson's relations to BNT hf. Hermann is a member of the board of directors of the Company. Einar Sveinsson, a member of the board of directors of the Company is also a member of the board of directors of Glitnir banki hf. which is the Listing Advisor and of BNT hf.

Langflug ehf., Naust ehf. and Urður ehf. have all made lock-up agreements with the Manager. Both Langflug ehf. and Urður ehf. have a lock-up on all their shares until 14 December 2007. Naust ehf. has lock-up on 1/2 of its shares until 14 December 2007, and lock-up on ¼ on its shares until 14 June 2007 but other parts of the shares are not subject to lock-up. The total number of shares subject to lock-up until 14 December 2007 is 449,629,630 and the total number of shares subject to lock up until 14 June 2007 is 37,037,037. This totals 486,666,667 shares or 48.7% of the total share capital. Information about the companies subject to lock-up on their shares is provided in sections 18.1.1, 18.1.3 and 18.1.4.

No other Director or member of senior management has any potential conflict of interest between their duties to the Company and their private interests or other duties.

15.4 CONFIRMATIONS

In the past five years none of the board members or members of the senior management have been:

- Convicted in relation to a fraudulent offence.
- Associated with companies that have gone into bankruptcy, receivership or liquidation.
- Subject to any official public incrimination and/or sanctions by any statutory or regulatory authority (including any designated professional body) or have ever been disqualified by a court from acting as a director or member of the administrative, management or supervisory bodies of a company or from acting in the management or conduct of the affairs of a company.

16 BOARD PRACTICES

16.1 THE BOARD OF DIRECTORS

The members of the board of directors are elected at the Annual General Meeting (or other shareholders' meetings).

No member of the Company's board of directors or management has stated his intention of leaving his post.

16.2 SERVICE CONTRACTS

No specific agreements providing for benefits upon termination of employment exist between the Company and the members of the senior management or the board of directors other than mentioned below.

Jón Karl Ólafsson, the CEO, has a notice period of 24 months. Other mentioned members of the management have a notice period of 12 months. The employment agreements contain no provisions for other retirement benefits.

16.3 AUDIT COMMITTEE AND WAGE TERMS COMMITTEE

The current board of directors has recently installed both an auditing committee and a wage terms committee.

The auditing committee will be appointed by the Company's board of directors. The current members of the committee are three members of the board of directors: Ómar Benediktsson (chairman), Jóhann Magnússon and Marta Eiríksdóttir. The main tasks of the committee include co-ordination on auditing within the Group, in co-operation with the Company's internal auditors, and acting in an advisory capacity to the board of directors with respect to report making.

The purpose of installing a wage terms committee is to avoid having the management control its own remuneration and furthermore to ensure that the management's remuneration is structured so as to serve the long-term interests of the shareholders. The main tasks of the wage terms committee are policy making with respect to the management's performance-related bonuses, including stock option purchases. The committee performs evaluations on the management's remuneration and monitors the management's stock purchases. The current members of the committee are three members of the board of directors: Finnur Ingólfsson (chairman), Hermann S. Guðmundsson and Helgi Sigurður Guðmundsson.

16.4 COMPLIANCE

The Company does not comply with the Guidelines of Corporate Governance issued by the Iceland Stock Exchange (ICEX), Iceland Chamber of Commerce and the Confederation of Icelandic Employers. Out of seven members of the board of directors, only three are independent.

17 EMPLOYEES, REMUNERATION AND BENEFITS

17.1 REMUNERATION AND BENEFITS

For the year 2006, Jón Karl Ólafsson's remunerations and benefits amounted to ISK 36 million. Jón Karl is the CEO of Icelandair Group and Icelandair ehf. For the same period, Hlynur Elísson, CFO, received ISK 18 million and Sigþór Einarsson, COO, ISK 27 million. No material changes regarding remuneration for these individuals have taken place from the year 2005.

Remuneration for the board of directors will be decided at annual general meetings which will be held before the end of May each year. However, from 1 November 2006 until the next annual shareholders meeting, all the members of the board of directors will be paid ISK 200,000 per month, except the chairman who will receive ISK 400,000 per month, as agreed by shareholders on the shareholders meeting on 15 November 2006. These figures represent all payments from Icelandair Group Holding, Icelandair Group and its subsidiaries to the Board members.

17.2 STOCK OPTION PLAN

The purpose of the stock option plan, approved by shareholders on the shareholders meeting on 29 December 2006, is to enable Icelandair Group to attract and retain employees through an attractive system of remuneration, particularly as regards the key personnel in the management and technological development of the Company, and at the same time provide such employees with an opportunity to acquire a share in the Company and thereby contribute to increased incentives and reward for promoting the increased growth and prosperity of the Company in the long term.

The stock option plan did take effect on 29 December 2006 and remains in effect while the authorization granted to the board of directors at the shareholders' meeting held on 29 December 2006 remains effective without change. Stock options granted to employees which have not been exercised shall in any case lapse four weeks after the annual general meeting of the company in 2010.

This stock option plan and its implementation fall under the authority and supervision of the wage terms committee of the Company pursuant to authorisation granted by the board of directors of the Company. The wage terms committee will decide the stock option of the CEO of the Company under this stock option plan, after which the wage terms committee, on the 3 recommendation of the CEO, will decide which employees of the Company and/or its subsidiaries qualify for stock options and thereby participation in the stock option plan and when stock options should be granted pursuant to contracts with individual participants. Furthermore, the wage terms committee shall decide on the specific terms of stock option contracts.

The authorisation of the board of directors to issue stock options is limited so that the outstanding options at any time must never amount to a higher proportion than 6% of the total shares in the Company at any time, currently shares in the nominal amount of ISK 60,000,000. The amount of the stock option of any single employee shall not exceed 10% of the total issued stock options. However, this rule shall not apply to the CEO of the Company. The Company can both use its own shares for options, purchase shares, or issue new shares as authorised by a shareholders' meeting, in order to meet Company obligations pursuant to stock option contracts.

On the delivery of stock options to employees, the Company shall enter into a written stock option contract with the employee. The terms and conditions of stock option contracts need not be uniform, and options may be adapted to individual employees.

SUMMARY SECURITIES NOTE REGISTRATION DOCUMENT

17.2.1 ISSUED STOCK OPTIONS FOR SENIOR MANAGEMENT

The board of directors of Icelandair Group Holding hf. (ICEAIR) decided on the basis of the company's stock option plan scheme to grant stock options on shares in Icelandair Group to its senior management. The options are valid until 9 January 2010.

Options to buy a total of 45.3 million shares were granted to a total of 17 senior management, including the CEO, vice president and managing directors of subsidiaries. Stock option holders are entitled to exercise one third of their stock option for 4 weeks, starting 3 January 2008, 2009 and 2010. The option has an exercise price of ISK 27.5 per share, which is the weighted average closing price on the Iceland Stock Exchange during the last ten trading days prior to the granting of the options. The stock option plan is primarily subject to the condition of the employee's conditioned employment with in the group.

17.3 PENSION LIABILITY

The total pension liability of Icelandair Group towards former employees amounts to ISK 53 million. No pension liability exists towards current Directors of the Board or management.

17.4 NUMBER OF EMPLOYEES

The Company believes that one of its principal strengths lies in its employees and the employees of its subsidiaries. Its operations require a wide range of knowledge and specialised personnel within aviation technology, international marketing, finance and management. Employee numbers since 2003 are presented in Table 14. Due to seasonal fluctuations, the Icelandair Group's subsidiaries employ more people during the summer than during other periods. In the summer 2006 the increase in total number of Icelandair Group's employees amounted to around 500-600 people. Most of this increase was due to increase in number of Icelandair's employees.

Table 14. Number of employees

	31/12 2003	**31/12 2004**	**31/12 2005**	**31/12 2006**
Icelandair Group	-	-	-	15
Icelandair	867	934	927	1154
Icelandair Ground Services (IGS)	337	432	492	522
ITS Technical Services	183	228	244	260
Icelandair Cargo	50	47	47	50
Loftleiðir-Icelandic ehf.	5	5	9	11
Bluebird Cargo	48	52	65	64
Icelease	-	-	-	1
Air Iceland	235	248	255	282
Icelandair Hotels	237	276	255	263
Iceland Travel	48	73	57	48
Icelandair Shared Services	55	59	81	77

There has been no material change in the number of employees since 31 December 2006.

Table 15. Geographical location of Icelandair Group´s employees

	31/12 2006
Iceland	2,587
USA	73
Scandinavia	32
Central-Europe	21
South-Europe	11
UK	20
Finnland	3

17.5 ARRANGEMENTS FOR INVOLVING THE EMPLOYEES IN THE SHARE CAPITAL

In the share offer for Icelandair Group Holding, from 27 November until 4 December 2006, all employees of Icelandair Group and its subsidiaries were given the opportunity to acquire certain amount of shares in the Company without being subject to reduction. In addition, Glitnir banki hf. offerd employees financing for share purchase on favourable terms.

As discussed in section 17.2 a stock option plan was approved by shareholders on the shareholders meeting on 29 December 2006, with the purpose of enabling Icelandair Group to attract and retain employees through an attractive system of remuneration, particularly as regards the key personnel in the management and technological development of the Company, and at the same time provide such employees with an opportunity to acquire a share in the Company and thereby contribute to increased incentives and reward for promoting the increased growth and prosperity of the Company in the long term.

18 SHAREHOLDERS

18.1 LIST OF MAJOR SHAREHOLDERS

Table 16. The 20 largest shareholders of the Company as of 6 February 2007

Name	Share capital	Share capital
Langflug ehf	320,000,000	32.0%
Naust ehf	148,148,148	14.8%
Fjárfestingafélagið Máttur ehf	111,111,111	11.1%
GLB Hedge	78,300,867	7.8%
Urður ehf	55,555,556	5.6%
Glitnir banki hf	41,148,073	4.1%
Flugval ehf	18,518,519	1.9%
Lífeyrissjóðir Bankastræti 7	14,769,600	1.5%
Samvinnulífeyrissjóðurinn	12,887,666	1.3%
Lífeyrissjóður verslunarmanna	11,111,111	1.1%
Saxbygg ehf	10,000,000	1.0%
Miðbæjareignir ehf	10,000,000	1.0%
Magt ehf	9,259,260	0.9%
Credit Suisse Securities(Eu)Ltd	9,000,000	0.9%
Lífeyrissjóður Austurlands	8,650,000	0.9%
Almenni lífeyrissjóðurinn	8,006,047	0.8%
Gildi -lífeyrissjóður	7,230,290	0.7%
Barclays Capital Securities Ltd.	7,000,000	0.7%
Glitnir Sjóðir hf,sjóður 10	6,844,954	0.7%
Sameinaði lífeyrissjóðurinn	5,799,407	0.6%
	893,340,609	89.3%

18.1.1 LANGFLUG EHF.

Langflug ehf. Icelandic ID No. 660906-1500, reg. office Suðurlandsbraut 18, 108 Reykjavík, Iceland is an investment company owned 75% by Eignarhaldsfélagið Samvinnutryggingar svf., Icelandic ID No. 550269-0589, reg. office Kringlan 7, 103 Reykjavík, Iceland and 25% by Finnur Ingólfsson, the chairman of the board of directors of the Company, Icelandic ID No. 080854-3829. Finnur Ingólfsson, is also a member of the board of directors of Langflug ehf. Langflug was founded by Kristinn Hallgrímsson hrl. acting as an attorney on behalf of Eignarhaldsfélagið Samvinnutryggingar svf.

Eignarhaldsfélagið Samvinnutryggingar svf. is a holding company with the purpose of participating in insurance related operations, purchases, sales and ownership of stocks and bonds, lending and real estates.

18.1.2 FJÁRFESTINGAFÉLAGIÐ MÁTTUR EHF.

Fjárfestingafélagið Máttur ehf., Icelandic ID No. 511105-1610, reg. office Suðurlandsbraut 12, 108 Reykjavík, Iceland, is an investment company owned 47.5% by Sjóvá hf., Icelandic ID No. 701288-1739, reg. office Kringlunni 5, 103 Reykjavík, Iceland, 5% by Gunnlaugur M. Sigmundsson, CEO of Fjárfestingafélagið Máttur ehf., Icelandic ID No. 300648-3719, Þverárseli 20, 109 Reykjavík, Iceland and 47.5% by Glitnir banki hf.

18.1.3 NAUST EHF.

Naust ehf., Icelandic ID No. 460906-0320, reg. office Suðurlandsbraut 18, 108 Reykjavík, Iceland is an investment company. The company is jointly owned by the following parties:

- BNT hf. Icelandic ID No. 530206-0250, reg. office Suðurlandsbraut 18, 108 Reykjavík, Iceland, owns 49.9% of the share capital in Naust ehf.
- Glitnir banki hf., Icelandic ID No.550500-3530, reg. office Krikjusandur, 155 Reykjavík, Iceland, owns 30.1% of the share capital in Naust ehf.
- Hrómundur ehf., Icelandic ID No. 491188-2519, reg. office Bakkaflöt 10, 210 Garðabæ, Iceland, owns 10.0% of the share capital in Naust ehf. Hrómundur ehf. is owned by Einar Sveinsson.
- Hafsilfur ehf., Icelandic ID No. 610469-0199, reg. office Lindarflöt 51, 210 Garðabæ, Iceland, owns 10.0% of the share capital in Naust ehf. Hafsilfur ehf. is owned by Benedikt Sveinsson.

It should be noted that Hrómundur ehf. owns a 2.6% share in Glitnir banki hf., Hafsilfur ehf. owns a 1.01% share in Glitnir banki hf. and Fjárfestingafélagið Máttur ehf. and Glitnir banki hf. each own 12% share in BNT hf.

18.1.4 URÐUR EHF.

Urður ehf., Icelandic ID No. 681290-1689, reg. office Austurstræti 5, 155 Reykjavík, Iceland, is owned 66.7% by Blue Sky Transport Holding S.A. a company owned 100% by Ómar Benediktsson, Icelandic ID No.221059-4689 and 33.3% by FSP hf. Icelandic ID No. 510400-2670, Skógarhlíð 12, 105 Reykjavík, Iceland.

Ómar Benediktsson is a member of the board of directors of the Company.

18.1.5 GLITNIR BANKI HF.

Glitnir banki hf., Icelandic ID No., 550500-3530, reg. office Kirkjusandur 2, 155 Reykjavík, Iceland. Glitnir banki hf. is the Listing Advisor and Glitnir banki hf. directly holds 45,416,707 shares.

- Glitnir banki hf. holds 47.5% of the share capital in Fjárfestingafélagið Máttur ehf., which holds 111,111,111 shares in Icelandair Group hf.

- Glitnir banki hf. directly holds 30.1% of the share capital in Naust ehf. which holds 148,148,148 shares in Icelandair Group hf. Glitnir banki hf. also holds 12% of the share capital in BNT hf., which holds 49.9% of the share capital in Naust ehf. Furthermore, Glitnir banki hf. holds 47.5% of the share capital in Fjárfestingafélagið Máttur ehf. which in turn has 12% ownership in BNT hf.

- All figures are as of 7 February 2007. Voting rights are held by the majority of each company directly owning shares in Icelandair Group.

The Company does not hold any shares in Glitnir banki hf. Einar Sveinsson, a member of the board of directors of the Company is also a member of the board of directors of Glitnir banki hf.

18.1.6 FLUGVAL EHF.

Flugval ehf., Icelandic ID No. 511006-0230, reg.office Funafold 97, 112 Reykjavík, Iceland, is owned 100% by Jón Karl Ólafsson, the CEO of Icelandair Group.

18.1.7 GLB HEDGE

GLB Hedge, Icelandic ID No 620906-9990, reg. office Kirkjusandur 2, 155 Reykjavík, Iceland holds shares to hedge Glitnir Banki hf.´s risk in connection with forward contracts.

18.2 SHARE DISTRIBUTION

The Company fulfils the condition regarding the number of shareholders and share distribution required for listing on the ICEX Main List.

18.3 VOTING RIGHTS

Each issued share carries one vote. Accordingly, major shareholders do not have voting rights that are different from those of other shareholders.

18.4 CHANGE IN CONTROL OF THE COMPANY

The Company does not know of any arrangements between shareholders or other parties that may result in a change in control of the Company.

18.5 DIRECT OR INDIRECT OWNERSHIP OR CONTROL BY INDIVIDUAL SHAREHOLDERS

The Company's management states that, to the extent known to the issuer, the Company is not directly or indirectly owned or controlled by parties other than the listed shareholders.

18.6 CONVERTIBLE BOND

Icelandair Group Holding hf. issued on the 24 October 2006, bonds in the nominal amount of ISK 2,000,000,000 that give the owner the right to convert the principal of the claim under the bonds to shares at the base rate of 29.7 which will be as amended in accordance with dividend payments and share capital increase as described in the articles of association of Icelandair Group Holding hf. With the Merger, the obligations under the bonds where taken over by the Company and provisions added to the Articles of Association of the Company to evidence this.

19 RELATED PARTY TRANSACTIONS

The board of directors of the Company believes that the Company's related party transactions described below are conducted on an arm's length basis.

Attention is drawn to Icelandair ehf's. recent agreement with Olíufélagið ehf. regarding fuel services for Icelandair at Keflavík Airport. This agreement was reached after seeking offers from all major oil distributors in Iceland. The majority owner of Olíufélagið ehf. is BNT hf. which also owns 49.9% share in Naust ehf., one of Icelandair Group main shareholders. It is the management's opinion that this agreement was reached at fair value. The amount relating to this agreement represents approximately 6.5% of the Icelandair's revenue.

Icelandair Group hf. and its subsidiaries have insurance agreements with Sjóva hf., who is one of the owners of Fjárfestingafélagið Máttur ehf, which is a shareholder in the Company. However, the amount relating to this agreement is less than 0.05% of the Company's turnover in 2005.

No other material transactions have taken place with related parties.

20 FINANCIAL INFORMATION

Information concerning the Company's financial position is presented in the following four sections. Information on the five largest subsidiaries of Icelandair Group is presented in section 21, containing each company's income statement, balance sheet and statement of cash flow for the years 2003-2005 and the first nine months of 2005 and 2006. Information on the Group's performance for the first 9 months of 2006 is given in section 22, discussion on pro forma statement of earnings for the year 2005 is in section 23 and the consolidated balance sheet for Icelandair Group dated 31 October 2006 is provided in section 24. The consolidated balance sheet is internally generated and the pro forma accounts are provided for illustrative purposes only.

20.1 IFRS

The financial statements of the companies that comprise Icelandair Group hf., for the years 2004 and 2005 and the first nine months of 2006 were prepared in accordance with International Financial Reporting Standards (IFRS) but 2003 was prepared in accordance with Icelandic GAAP.

20.2 EXPLANATORY NOTES

Detailed information regarding the items in the income statements, cash flow and balance sheets are accessible in the policies and explanatory notes in each annual and interim report available via the Appendix.

20.3 DIVIDEND POLICY

From the time of incorporation on 20 December 2005, no dividends have been paid. It should also be noted that Icelandair Group hf. did not pay any dividends because of the financial year 2005.

The Company's board of directors has the intention to set a policy of paying 35-50% of each year's earnings before interest and taxes in dividends to shareholders.

20.4 OPERATING INCOME AND EXPENCES

20.4.1 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.

20.4.2 AIRCRAFT AND AIRCREW LEASE

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

20.4.3 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.

20.4.4 OPERATING LEASE PAYMENTS

Payments made under operating leases are recognised in the income statement on a straight-line basis over the term of the lease.

20.5 SIGNIFICANT CHANGE IN THE COMPANY'S FINANCIAL POSITION

The purchase of Icelandair Group hf. by Icelandair Group Holding hf. resulted in a significant change in the Group's financial positions. These changes are accounted for in section 23 by pro-forma accounts adjusting for the purchase and the subsequent merger of the two companies.

On 24 October 2006, Icelandair Group Holding issued bonds in the nominal amount of ISK 2,000,000,000 that give the owner the right to convert the principal of the claim under the bonds to shares in Icelandair Group as described in section 27.2.

In early November 2006, the Company agreed to purchase two Boeing 737-400 aircraft as discussed in section 14.2.1. and in December 2006 the Company signed a letter of intent to purchase two Boeing 757-200 aircraft. These purchases will result in increased borrowing requirements as mentioned in section 26.1. Other significant changes have not occurred since the last interim report.

21 SELECTED SUBSIDIARIES

This section provides a description of the financial condition of the Company's five most important subsidiaries, which combined represent around 88% of the Company's turnover for the years 2003, 2004 and 2005 and the first nine months of 2005 and 2006 for all the five subsidiaries.

Accounts for 2003, 2004 and 2005 were audited. The interim accounts for the first nine months of 2005 were not audited but are, in this document, presented in the same form as annual accounts. The income statements, balance sheets and statements of cash flow for the first nine months of 2006 were audited.

21.1 ICELANDAIR

Icelandair's revenue in 2005 amounted to ISK 31.5 billion, roughly 76% of which is transport revenue, i.e. transportation of people and freight. Revenues increased by ISK 5.8 billion or 22% from 2003 to 2005. Approximately 75% of the revenue is in foreign currency and as the ISK strengthened by 14% from 2003 to 2005, revenue on fixed rate increase was more than 22%. The revenue increase is mainly due to an increase in passenger numbers. The number of passengers travelling from Iceland increased by 42% and the number of passengers travelling via Iceland increased by 48%. Further, the airline added fuel surcharge to ticket prices in mid 2004 to meet higher fuel prices. Loftleiðir-Icelandic hf. and Icelandair Cargo operate under Icelandair's AOC and thus all aircraft operating costs of these firms are registered in Icelandair's books which are later charged to the companies. These transactions are netted out in Icelandair Group's statement of income.

Capacity has been increasing in recent years and available seat kilometres in the company's flight schedule increased by 28% from 2003 to 2005. Total costs in 2005 increased by ISK 5.6 billion or 22% compared to 2003, mainly due to higher fuel prices. Together with more activity the over 93% increase in fuel prices from 2003 to 2005 explains the cost increase. Excluding fuel costs operational costs increased by 11% from 2003 to 2005. Therefore, Icelandair's costs per available seat kilometres, excluding fuel costs, has decreased by 15% from 2003 to 2005 which is primarily attributable to the ISK appreciation as roughly 75% of the companies costs are in foreign currencies.

EBITDA totalled ISK 980 million for the year 2005 which is a ISK 180 million increase since 2003. EBIT was ISK 296 million in 2005 which is ISK 379 million lower than in 2003 due to more depreciation. The decrease is a result of changes in accounting methods, e.g. an overhaul in owned aircraft engines is booked as maintenance costs in both 2003 and 2004 but in 2005 the overhaul were booked as assets and depreciated.

Icelandair's revenue in the first nine months of 2006 totalled ISK 29.5 billion and approximately 76% of the revenues are related to the transportation of people and freight. The revenue increase was ISK 5.2 billion or 21%

from the same period in 2005. The increase is mostly attributable to more revenues from passenger travel and an increase of the fuel surcharge in line with fuel cost increase. Further, the ISK has depreciated in the period and thus revenues, in ISK terms, were higher. Increase in revenue due to intra company business is approximately 27%.

Available seat kilometres in the company's flight schedule were almost as many as in the same period of 2005. The company's costs amounted to ISK 26.4 billion. The operational costs increased by ISK 3.4 billion or 15% from the same period in previous year. Excluding fuel costs the costs increased 9% from the same period the year before. The increase is mostly attributable to higher personnel costs, e.g. a company wide payroll changes on 1 July 2006, as well as increased maintenance following the lease of aircraft and large scale maintenance checks. Further, the ISK depreciation in the period increases costs in ISK. Aircraft rental costs are lower as the company purchased aircraft which were previously leased from FL Group. Leasing cost in 2005, for the aircraft the company now owns, was ISK 1,116 million.

The company leases most of the operating assets it requires in its business. At 31 December 2005 total assets amounted to ISK 11,662 million compared to ISK 9,502 million in 2003. This 23% increase comes almost all from an increase in outstanding trade and other receivables which can be explained with 23% revenue turnover increase over same period.

Assets from 31 December 2005 until 30 September 2006 increased considerably mainly due to the purchase of operating assets, including aircraft and real estate from FL Group. The purchases were financed by taking over liability obligations in the amount of ISK 12,000 million and ISK 3,000 million internally with equity. This furthermore explains the increase in the company's debt.

Equity at year end 2005 is ISK 3,642 million of which share capital is ISK 3,000 million.

The cash flow from operating activities reflects cash generous operations. On regular the company collects money from its customers before service is provided. As the company was established in 2003, the company invested heavily that year in operating assets. Cash from operating activities at year end 2005 amounted to ISK 2,781 million, cash used in investing activities, mainly engine overhaul, amounted to ISK 629 million and cash from financing activities amounted to ISK 1,126 million leaving cash at year end 2005 at ISK 6,542 million.

Operating cash at 30 September 2006 is ISK 5,082 million, which is an increase by ISK 1,580 million from the same period in 2005. Net capital investment is ISK 21,226 million and financing activities are positive by ISK 11,315 million due to new liabilities. Cash and cash equivalents decreases from year end 2005 until 30 September 2006 by ISK 4,829 million and is ISK 1,713 million.

Icelandair paid dividends in April 2004 in the amount of ISK 525 million.

Table 17. The following table is based on audited Income Statements of Icelandair for 2003-2005 and for the first nine months of 2006 and the Income Statement for the first nine months of 2005. All figures in ISK million.

	2003 1/1-31/12	2004 1/1-31/12	2005 1/1-31/12	2005 1/1-30/9	2006 1/1-30/9
Operating income:					
Transport revenue	18,161	20,409	23,818	18,805	22,408
Aircraft and aircrew lease	4,991	6,968	6,161	4,450	5,682
Other operating revenue	2,548	1,680	1,484	1,069	1,437
Net operating income:	25,700	29,057	31,463	24,324	29,527
Operating expenses:					
Salaries and other personnel expenses	6,401	7,572	8,451	6,252	6,901
Aircraft fuel	3,442	5,352	6,740	5,050	6,899
Aircraft and aircrew lease	3,348	3,108	3,228	2,411	1,907
Aircraft servicing, handling and communication	3,922	4,555	3,786	2,999	3,490
Aircraft maintenance expenses	2,528	2,333	2,827	2,128	2,579
Other operating expenses	5,259	5,061	5,451	4,135	4,630
Net operating expenses:	24,900	27,981	30,483	22,975	26,406
Operating profit before depreciation and rent (EBITDAR)	4,148	4,184	4,208	3,760	5,028
Operating profit before depreciation (EBITDA)	800	1,076	980	1,349	3,121
Depreciation	(125)	(691)	(684)	(528)	(949)
Operating profit before net financial income (EBIT)	675	385	296	821	2,172
Net financial income (expenses)	(62)	(258)	261	4	505
Profit before tax	613	127	557	825	2,677
Income tax expense	(111)	(28)	(108)	(155)	(488)
Profit	502	99	449	670	2,189

Table 18. The following table is based on Icelandair's audited Balance Sheet on 31 December 2003-2005 and on September 30, 2006. All figures in ISK million.

	2003 31/12	2004 31/12	2005 31/12	2006 30/09
Assets:				
Operating assets	1.296	1.598	1.622	15.215
Intangible assets	70	110	121	186
Investments in associates	7	4	2	4
Long-term receivables	309	296	244	524
Total non-current assets	1.682	2.008	1.989	15.929
Inventories	158	172	156	221
Trade and other receivables	2.720	2.082	2.060	3.464
Intra company receivables	698	1.813	915	1.020
Interest bearing intra company receivables				6.662
Cash and cash equivalents	4.244	3.264	6.542	1.713
Total current assets	7.820	7.331	9.673	13.080
Total assets	9.502	9.339	11.662	29.009
Equity:				
Share capital	3.000	3.000	3.000	3.000
Reserves	50	(31)	87	189
Retained earnings	226	151	555	2.744
Total equity	3.276	3.120	3.642	5.933
Liabilities:				
Deferred income tax liability	140	153	89	577
Credit institutions				10.254
Total non-current liabilities	140	153	89	10.831
Crediti institutions				1.165
Intra company loans				508
Trade and other payables	4.512	4.428	5.838	7.124
Prepaid income	1.574	1.638	2.093	3.449
Total current liabilities	6.086	6.066	7.931	12.245
Total liabilities	6.226	6.219	8.020	23.076
Total equity and liabilities	9.502	9.339	11.662	29.009

Table 19. The following table is based on Icelandair's audited Cash Flow Statements for the years 2003, 2004 and 2005 and the first nine months of 2006 and the Cash Flow Statement for the first nine months of 2005. All figures in ISK million.

	2003 1/1-31/12	2004 1/1-31/12	2005 1/1-31/12	2005 1/1-30/9	2006 1/1-30/9
Cash flow from operating activities:					
Profit	502	99	449	670	2,189
Adjustments for:					
Depreciation	125	691	684	528	949
Other operating items	994	173	62	160	319
Working capital from operations	1,621	963	1,195	1,358	3,457
Net change in operating assets and liabilities	2,210	501	1,586	2,144	1,625
Net cash from operating activities	3,831	1,464	2,781	3,502	5,082
Cash flow from investing activities					
Acquisition of operating assets	(2,343)	(563)	(594)	(198)	(14,682)
Acquisition of intangible assets		(101)	(90)	(141)	(134)
Proceeds from the sale of assets	4	1	4	3	
Investments	(248)	36	51	24	(250)
Intra company interest bearing receivables					(6,160)
Net cash used in investing activities	(2,587)	(627)	(629)	(312)	(21,226)
Cash flow from financing activities:					
Dividends paid		(525)			
Proceeds from issue of share capital	3,000				
New long term debt					12,273
Repayment of borrowings					(879)
Short term receivables, change					42
Interest bearing loan due to parent company		(1,292)	1,126		(121)
Net cash used in financing activities	3,000	(1,817)	1,126		11,315
Increase (decrease) in cash and cash equivalents	4,244	(980)	3,278	3,190	(4,829)
Cash and cash equivalents at January 1		4,244	3,264	3,264	6,542
Cash and Cash equivalents at the end of period	4,244	3,264	6,542	6,454	1,713

21.2 ICELANDAIR CARGO

Icelandair Cargo's operating income for the year 2005 amounted to ISK 4.6 billion, increasing by ISK 665 million or 17% from 2003. This increase can be explained by increased income from both import and export and by income from operations for the delivery company TNT that did not exist in 2003. In addition other income factors, such as fuel and insurance surcharges, have increased. In 2005 larger freight aircraft were in operations than in 2003. However, due to the delay of delivery of two aircraft being modified for cargo operations, operating income increased less than could have been expected. The company's revenue decreased by ISK 191 million or 4% from 2004 to 2005, caused mainly by less exports to USA and Europe resulting from the strength of the ISK currency.

Operating expenses for the year 2005 amounted to ISK 4.6 billion, increasing by ISK 827 million from 2003. This increase can be explained by increased cost relating to larger fleet and the cost related to the for mentioned delay of two aircraft from modification. Additionally, crew related expenses and maintenance costs increased over the period as did fuel costs.

Approximately 6% of Icelandair Cargo's expenses are due to intra Group transactions. This is explained by transportation of cargo for ITS and IGS and sale of cargo space to Bluebird Cargo.

EBIT amounted to ISK 6 million in 2005 compared to ISK 182 million in 2003.

For the first nine months of 2006, Icelandair Cargo's operating income came to ISK 4.8 billion, increasing by 47% from the first nine months of 2005. This increase is mostly due to increased number of flights and larger fleet. In the first nine months of 2006, the company had on average 3.6 aircraft in operation compared to 2.4 aircraft in the first nine months of 2005. Imports increased largely because of a new agreement with the delivery company TNT and the effects of the agreement with TNT were not fully effective in the first nine months of 2005. Income from leasing activities was also greater in the first nine months of 2006 compared to the same period in 2005.

Operating expenses amounted to ISK 4.6 billion for the first nine months of 2006, increasing by 45% from the same period in 2005. Larger fleet, increased number of flights and increasing fuel prices explain most of this increase.

In the first nine months of 2006, EBIT amounted to ISK 131 million compared to ISK 27 million in the same period 2005.

The company leases most of the operating assets it requires in its business. At 31 December 2005 total assets amounted to ISK 1,014 million compared to ISK 877 million at the end of 2003. This 16% increase comes all from an increase in outstanding trade and other receivables which can be explained with 17% revenue turnover increase over same period.

Assets did increase by 22% from year end 2005 until 30 September 2006. This can be explained by 48% increase in revenues resulting in an increase in outstanding trade and other receivables.

Total equity is similar in 2003 and 2005 since the company paid ISK 236 million, retained earnings, in dividends to the Parent for the years 2003 and 2004. Liabilities increased by 16% from year end 2003 until 31 December 2005 and by 12% from year end 2005 until 30 September 2006. This reflects the growing operation.

The company does not invest in assets as it leases them, therefore the cash flow from operating activities reflects the profit or loss for each year. At year end 2005 the cash from operating activities amounted to ISK 18 million.

Net cash used in investing activities amounted to ISK 18 million and cash used in financing activities came to ISK 71 million.

Operating cash at 30 September 2006 is ISK 2 million, which is a decrease by ISK 100 million from the same period in 2005, which can be explained by an increase by ISK 160 million in receivables, compared to an ISK 28 million increase in short term liabilities. Net capital investment is ISK 43 million and financing activities are positive by ISK 80 million due to new liabilities. Cash and cash equivalents increases from year end 2005 until 30 September 2006 by ISK 35 million and is ISK 211 million.

Icelandair Cargo paid dividends in April 2004 and 2005 in the amount of ISK 10 million and 226 million respectively.

Minority shareholdings are due to Icelandair Cargo's ownership in Icelandair Logistics SA.

Table 20. The following table is based on the audited Income Statements of Icelandair Cargo for the years 2003-2005 and the first nine months of 2006 and the Income Statement for the first nine months of 2005. All figures in ISK million.

	2003 1/1-31/12	**2004 1/1-31/12**	**2005 1/1-31/12**	**2005 1/1-30/9**	**2006 1/1-30/9**
Operating income:					
Cargo and mail	2,698	3,207	3,053	2,203	2,923
Aircraft lease	436	442	282	166	710
Service revenue	759	1,096	1,213	876	1,126
Other operating revenue	23	27	34	20	40
Net operating income:	3,916	4,772	4,581	3,264	4,800
Operating expenses:					
Aircraft operating expenses	2,762	3,422	3,502	2,463	3,683
Warehouse related expenses	392	431	414	316	427
Delivery expenses	105	123	92	66,525	93
Salaries and other personnel expenses	219	240	294	185,553	240
Sales and marketing expenses	74	80	64	56	52
Administrative expenses	171	153	184	131	159
Net operating expenses:	3,723	4,449	4,550	3,218	4,654
Operating profit before depreciation (EBITDA)	193	323	32	46	145
Depreciation	(12)	(21)	(26)	(19)	(14)
Operating profit before net financial income (EBIT)	181	302	6	27	131
Net financial income (expenses)	38	(1)	3	(2)	15
Profit before tax	219	301	9	25	146
Income tax expense	(1)	(55)	(2)	(5)	(28)
Profit	218	246	7	20	118

Table 21. The following table is based on Icelandair Cargo's audited Balance Sheet on 31 December, 2003, 2004 and 2005 and the Balance Sheet on 30 September 2006. All figures in ISK million.

	2003 31/12	2004 31/12	2005 31/12	2006 30/09
Assets:				
Operating assets	16	12	26	49
Intangible assets	20	24	13	19
Insurance fees		11		
Total non-current assets	36	47	39	68
Trade and other receivables	672	665	798	928
Intra company receivables				21
Prepaid cost			1	9
Cash and cash equivalents	168	247	176	211
Total current assets	840	912	975	1.169
Total assets	877	958	1.014	1.237
Equity:				
Share capital	100	100	100	100
Share reserve		25	25	25
Translation reserves		1		1
Retained earnings	15	227	7	125
	115	352	132	251
Minority shareholdings		2		(3)
Total equity	115	354	133	248
Liabilities:				
Deferred income tax liability	1	8	7	7
Total non-current liabilities	1	8	7	7
Credit institutions			11	91
Trade and other payables	351	439	307	456
Intra company payables	410	157	556	435
Total current liabilities	761	596	875	982
Total liabilities	762	604	882	989
Total equity and liabilities	877	958	1.014	1.237

Table 22. The following table is based on Icelandair Cargo's audited Cash Flow Statement for the years 2003, 2004 and 2005 and the Cash Flow Statement for the first nine months of 2005 and 2006. All figures in ISK million.

	2003 1/1-31/12	2004 1/1-31/12	2005 1/1-31/12	2005 1/1-30/9	2006 1/1-30/9
Cash flow from operating activities:					
Profit for the period	218	246	7	20	118
Adjustments for:					
Depreciation	12	21	26	19	14
Other operating items	(12)	5	(1)	3	
Working capital from operations	218	272	31	42	132
Net change in operating assets and liabilities	193	(110)	(13)	56	(134)
Net cash from operating activities	411	162	18	98	(2)
Cash flow from investing activities					
Acquisition of operating assets	(6)	(3)	(25)	(24)	(30)
Acquisition of intangible assets	(38)	(5)	(3)	(3)	(10)
Long-term receivables, change		(10)	11	1	(3)
Net cash used in investing activities	(43)	(18)	(18)	(26)	(43)
Cash flow from financing activities:					
Dividends		(10)	(226)	(226)	
Repayment of long-term borrowings	(79)	(56)			
Short-term borrowings, change	(241)		11		
Interest bearing loan due to parent company			144	14	80
Net cash used in financing activities	(320)	(66)	(71)	(212)	80
Increase (decrease) in cash and cash equivalents	48	79	(71)	(140)	35
Cash and cash equivalents at January 1	120	168	247	247	176
Cash and Cash equivalents at December 31	168	247	176	107	211

21.3 LOFTLEIÐIR-ICELANDIC

It should be noted that Loftleiðir-Icelandic reports in USD and all figures below, both in the text and in the tables, have been converted from USD to ISK. In the profit and loss account the conversion rate is the average exchange rate over the accounting period and for the balance sheet the conversion rate is the exchange rate on 31 December, of each year, as published by Landsbanki Íslands hf. Loftleiðir-Icelandic's audited annual reports and interim reports in USD may be found in the Appendix.

Loftleiðir-Icelandic's operating income for the year 2005 amounted to ISK 5.6 billion, representing an increase of ISK 1.7 billion or 43% from the year 2003. For the same period, operating expenses increased by ISK 1.1 billion or 26% and were ISK 5.2 billion in the year 2005.

EBITDA in 2005 amounted to ISK 361 million, increasing by ISK 605 million from 2003. EBIT came to ISK 357 million in 2005 compared to negative ISK 246 million in 2003.

Improved operating results can be explained by better utilization of the company's aircraft, less deduction of receivables in addition to increased demand resulting in higher prices. The structure of the company's operation has also shifted from all inclusive leasing agreements to so called ACMI (Aircraft, Crew, Maintenance, Insurance) agreements, which has proven to provide better operating results.

The addition of Boeing 767 aircraft to the company's assets has also provided increased operating income. The demand for Boeing 767 aircraft has been high and more stable over the year than the other aircraft the company had in operations.

Approximately 1% of the company's operating revenue are intra group related, resulting from aircraft leasing to Icelandair.

For the first nine months of 2006 Loftleiðir-Icelandic's operating income amounted to ISK 5.4 billion, increasing by 1.2 billion or 29% from the same period in 2005. EBIT amounted to ISK 280 million in the first nine months of 2006 compared to ISK 288 million for the first nine months of 2005.

In June 2006 Loftleiðir-Icelandic purchased majority shares in The Latvian operator LatCharter who operates two Airbus 320´s on Wet Lease and Charter operations. The revenue increase by Loftleiðir connected to that is ISK 825 million. In 2006 the company returned one Boeing 767-300 aircraft and sold another Boeing 767-300. The sales profit was booked as extraordinary revenue and explains approximately ISK 387 million revenue increase between years. In addition the exchange rate for USD was 11% higher than at the same time in 2005.

The cost by Loftleiðir was ISK 5.1 billion in the first nine months of 2006 compared with ISK 3.9 billion in the same period in 2005. The biggest part can be explained by the acquisition of LatCharter (approximately ISK 935 million). In return for the two Boeing 767-300 aircraft the company introduced two new aircraft to the fleet, a Boeing 767-300 and a Boeing 757-200. The introduction cost of these aircraft has a negative effect on both the overall production and the financial performance of the company in the first nine months as a considerable investment was necessary in order to bring both aircraft up to standards (approximately ISK 90 million). Both aircraft were however leased in at considerably favourable terms which the company will benefit from in near future. In addition to this cost increases because of the weaker ISK versus USD.

In December 2006 LatCharter purchased two Airbus 320 aircraft. Both aircraft have been leased to Israir on a three year contract. One of the two aircraft was sold with a profit before the end of 2006.

The company leases most of the operating assets it requires in its business. At 31 December 2005 total assets amounted to ISK 1,172 million compared to ISK 424 million at 2003 year end. The increase comes mainly from operating profits these years which are still in the company.

Increase in operating assets from 31 December 2005 until 30 September 2006 can be explained by the purchase of LatCharter, which increased goodwill by ISK 889 million. In addition to this, the company prepaid aircraft leases in the amount of ISK 251 million. Finally, the change in working capital can be explained by the incorporation of LatCharter’s Balance Sheet into Loftleiðir-Icelandic’s accounts.

The company’s debt increased by ISK 1,256 million or 115% from 31 December 2005 until 30 September 2006, mainly due to the incorporation of LatCharter’s Balance Sheet into Loftleiðir-Icelandic’s accounts. Additionally, ISK 405 million of the purchase price of LatCharter are still to paid. Prepaid income increases by ISK 228 million.

The cash flow from operating activities reflects a very cash generous operation. On regular the company collects money from its customers before service is provided. Net cash from operating activities amounted to ISK 522 million at year end 2005.

Operating cash at 30 September 2006 is ISK 31 million, which is a decrease by ISK 382 million from the same period in 2005. This can mostly be explained by the costs associated with the modification of two aircraft. Cash and cash equivalents decreases from year end 2005 until 30 September 2006 by ISK 43 million and amount to ISK 597 million.

Loftleiðir-Icelandic paid no dividends for the years covered by historical financial information.

Table 23. The following table is based on the audited Income Statement of Loftleiðir-Icelandic for 2003-2005 and the Income Statement for the first nine months of 2005 and 2006. All figures in ISK millions. Accounts for 2004 and 2005 and first nine months for 2005 and 2006 were reported in USD and are adjusted according to the average rate of USD/ISK for each period.

	2003 1/1-31/12	2004 1/1-31/12	2005 1/1-31/12	2005 1/1-30/9	2006 1/1-30/9
Operating income:					
Aircraft and air crew lease	3,902	5,454	5,573	4,161	4,947
Sale of assets					411
Other operating revenue	14	19	36	25	29
Net operating income:	3,915	5,473	5,609	4,186	5,387
Operating expenses:					
Aircraft operating expenses	3,765	5,022	4,980	3,737	4,662
Passenger services	177	134	89	59	63
Salaries and other personel expenses	39	56	116	53	154
Administrative expenses	179	153	63	46	213
Net operating expenses:	4,160	5,365	5,248	3,895	5,092
Operating profit (loss) before depreciation (EBITDA)	(244)	108	361	291	295
Depreciation	(2)	(5)	(4)	(3)	(15)
Operating profit (loss) before net financial income (EBIT	(246)	103	357	288	280
Net financial income(expenses)	15	(18)	(32)	(27)	54
Profit (loss) before tax	(231)	85	325	261	334
Income tax expense	73	(15)	(60)	(49)	(41)
Profit (loss)	(158)	70	265	212	294

Table 24. The following table is based on Loftleiðir Icelandic's audited Balance Sheet on 31 December 2003, 2004 and 2005 and the audited Balance Sheet on 30 September 2006. All figures in ISK millions. Accounts for 2004, 2005 and 2006 were reported in USD and are adjusted according to the rate of USD/ISK on 31 December for each year.

	2003 31/12	2004 31/12	2005 31/12	2006 30/09
Assets:				
Operating assets	13	15	14	38
Intangible assets				890
Insurance fees				251
Tax assets	73	6	6	6
Total non-current assets	86	21	20	1.184
Inventories				16
Interest bearing intra company receivables			447	99
Trade and other receivables	118	100	185	775
Cash and cash equivalents	220	433	521	597
Total current assets	338	533	1.152	1.487
Total assets	424	554	1.172	2.671
Equity:				
Share capital	4	4	4	4
Share reserve			1	1
Other equity			38	(9)
Retained earnings (Accumulated deficit)	(332)	(225)	34	324
Total equity	(328)	(221)	77	320
Liabilities:				
Credit institutions				77
Trade and other payables	95	72	177	969
Intra company payables	495	418	564	699
Aircraft lease insurance deposits	41	130	134	176
Tax deficit		21	58	41
Prepaid income	121	134	162	390
Total liabilities	752	775	1.095	2.351
Total equity and liabilities	424	554	1.172	2.671

Table 25. The following table is based on Loftleiðir-Icelandic's audited Cash Flow Statement for the years 2003, 2004 and 2005 and for the first nine months of 2006 and the Cash Flow Statement for the first nine months of 2005. All figures in ISK millions. Accounts for 2004, 2005 and 2006 were reported in USD and are adjusted according to the average rate of USD/ISK for each period.

	2003 **1/1-31/12**	**2004** **1/1-31/12**	**2005** **1/1-31/12**	**2005** **1/1-30/9**	**2006** **1/1-30/9**
Cash flow from operating activities:					
Profit (loss)	(158)	70	265	212	294
Adjustments for:					
Depreciation	2	5	4	3	15
Profit (loss) from sale of assets	(73)	1			(411)
Other operating items	(7)	(9)	1	109	
Working capital from operations	(236)	67	270	324	(102)
Net change in operating assets and liabilities	294	225	252	105	133
Net cash from operating activities	58	292	522	429	31
Cash flow from investing activities:					
Acquisition of operating assets	(9)	(13)	(3)	(3)	(1,476)
Acquisition of intangible assets					(372)
Proceeds from the sale of assets		3			1,868
Acquisition of subsidiaries, less cash acquired					119
Short term receivables, change					(98)
Intra company receivables, change			(445)		
Net cash used in investing activities	(9)	(10)	(448)	(3)	41
Cash flow from financing activities:					
Borrowings, change					30
Net cash from financing activities					30
Increase (decrease) in cash and cash equivalents	49	282	74	426	102
Cash and cash equivalents at January 1	171	220	433	433	521
Effect of exchange rate fluctuations on cash held		(69)	14	15	(26)
Cash and Cash equivalents at December 31	220	433	521	844	597

21.4 BLUEBIRD CARGO

It should be noted that Bluebird Cargo reports in USD and all figures below, both in the text and in the tables, have been converted from USD to ISK. In the profit and loss account the conversion rate is the average exchange rate over the accounting period and for the balance sheet the conversion rate is the exchange rate on December 31, of each year, as published by Landsbanki Íslands hf. Bluebird Cargo's annual and interim reports in USD may be found in the Appendix.

Operational revenues amounted to ISK 2.3 billion in 2005, an ISK 767 million increase or 51% from 2003. Total costs were ISK 1.8 billion, which is an increase of ISK 846 million or 92% from 2003. EBIT results were ISK 273 in 2005 million compared to ISK 324 million in 2003.

In the beginning of 2003 Bluebird Cargo operated two Boeing 737-300 freight aircraft. In the end of 2003 two Boeing 737-300 freight aircraft were added to the fleet and a fifth in the start of 2005. All five freight aircraft are operated through fixed lease projects abroad and one aircraft serves the Icelandic freight market as well.

The revenue increase during the period is attributable to more aircraft in operation, more assignments, and sales of freight capacity to and from Iceland. The operational costs have increased in line with more activity

Revenue in the first nine months of 2006 amounted to ISK 2.2 billion which is an increase of ISK 459 million or 27% from the same period in 2005. Total costs in the period were ISK 1.6 billion, a ISK 273 million or 20% increase from the year before. EBIT decreased from ISK 324 million in 2003 to ISK 273 million in 2005.

Better results are due to increased revenue and synergies from the merger of Bluebird Cargo and Flugflutningar ehf. Further, the flight schedule was reorganized which yielded considerably better utilization and improved margins.

Bluebird Cargo's total operating assets came to ISK 2.4 billion at year end 2005 compared to ISK 2.7 billion at the end of 2003. Aircraft and aircraft related assets were 80% of assets in 2005 and 85% in 2003.

Assets did increase by 21% from year end 2005 until 30 September 2005. This can be explained by 27% increase in revenues. The reason behind the increase in both assets and liabilities is the merger of Flugflutningar hf. into Bluebird Cargo on 1 January 2006.

Equity increased by ISK 327 million from 31 December 2003 to 31 December 2005, which can be explained by new equity and retained earnings. No dividends were paid out for the year 2005.

Long term debt decreased by 48.9% from year end 2005 to 30 September 2006. The decrease is mainly due to difference in the USD/ISK exchange rate.

At year end 2005 the cash from operating activities amounted to ISK 438 million. Net cash used in investing activities amounted to ISK 308 million and cash used in financing activities came to ISK 253 million. Operating cash at 30 September 2006 is ISK 570 million, which is an increase by ISK 275 million from the same period in 2005. Net capital investment is ISK 300 million and cash flow from financing activities is negative by ISK 178 million due to the repayment of non current liabilities. Cash and cash equivalents increases from year end 2005 until 30 September 2006 by ISK 104 million and amount to ISK 219 million.

Bluebird Cargo paid no dividends for the years covered by historical financial information.

Table 26. The following table is based on the audited Income Statement of Bluebird Cargo for 2003-2005 and for the first nine months of 2006 and the Income statement for the first nine months of 2005. All figures in ISK millions. Accounts were reported in USD and are adjusted according to the average rate of USD/ISK for each period.

	2003 1/1-31/12	2004 1/1-31/12	2005 1/1-31/12	2005 1/1-30/9	2006 1/1-30/9
Operating income:					
Sales income	1,490	2,136	2,241	1,702	2,164
Other revenue	5	74	21	18	15
Net operating income:	1,495	2,210	2,262	1,720	2,179
Operating expenses:					
Salaries, aircrew lease and other personnel expense	245	371	415	323	413
Aircraft maintenance expenses	121	250	248	201	221
Aircraft lease	55	185	400	295	350
Aircraft fuel	145	215	265	193	202
Other operating expenses	354	479	438	347	446
Net operating expenses:	920	1,500	1,766	1,359	1,632
Operating profit before depreciation (EBITDA)	575	710	496	361	547
Depreciation	(251)	(269)	(223)	(186)	(193)
Operating profit before net financial income (EBIT)	324	441	273	175	354
Net financial income (expenses)	(174)	(145)	(115)	(90)	(78)
Profit before tax	150	296	158	85	276
Income tax expense	(5)	(47)	(35)	(21)	(50)
Profit	145	249	123	64	226

Table 27. The following table is based on Bluebird Cargo's audited Balance Sheet on 31 December, 2003, 2004 and 2005 and the audited Balance Sheet on 30 September 2006. All figures in ISK million. Accounts were reported in USD and are adjusted according to the average rate of USD/ISK for each period.

	2003 31/12	2004 31/12	2005 31/12	2006 30/09
Assets:				
Operating assets	2.266	1.758	1.941	2.255
Long term receivables	153	209	172	204
Total non-current assets	2.419	1.967	2.113	2.459
Inventories	1	3	7	10
Trade receivables	91	133	130	199
Other receivables	55	94	44	27
Cash and cash equivalents	89	232	115	219
Total current assets	236	462	296	455
Total assets	2.655	2.429	2.409	2.914
Equity:				
Share capital	351	323	333	370
Share reserve		26	39	43
Other equity	26	64	66	74
Retained Earnings	90	238	356	622
Total equity	467	651	794	1.109
Liabilities:				
Credit institutions	1.854	1.344	1.170	542
Deferred Income Taxes	5	40	76	96
Total non-current liabilities	1.859	1.384	1.246	637
Trade and other payables	98	78	99	205
Current maturities of non-current liabilities	205	247	215	821
Other current liabilities	26	69	55	141
Total current liabilities	329	394	369	1.167
Total liabilities	2.188	1.778	1.615	1.805
Total equity and liabilities	2.655	2.429	2.409	2.914

Table 28. The following table is based on Bluebird Cargo's audited Cash Flow Statement for the years 2003, 2004 and 2005 and for the first nine months of 2006 and the Cash Flow Statement for the first nine months of 2005. All figures in ISK millions. Accounts were reported in USD and are adjusted according to the average rate of USD/ISK for each period.

	2003 1/1-31/12	2004 1/1-31/12	2005 1/1-31/12	2005 1/1-30/9	2006 1/1-30/9
Cash flow from operating activities:					
Profit for the period	145	249	123	64	226
Adjustments for:					
Depreciation	251	269	223	186	193
Other operating items	5	25	31	21	49
Working capital from operations	401	543	377	271	468
Net change in operating assets and liabilities	6	(75)	61	24	102
Net cash from operating activities	407	468	438	295	570
Cash flow from investing activities					
Acquisition of operating assets	(6)	(52)	(353)	(292)	(289)
Pre payments	(117)	(90)	45	(53)	(11)
Net cash used in investing activities	(123)	(142)	(308)	(345)	(300)
Cash flow from financing activities:					
Dividends		(17)			
Repayment of long-term borrowings	(274)	(204)	(253)	(148)	(178)
Increase in equity	74	74			
Net cash used in financing activities	(200)	(147)	(253)	(148)	(178)
Increase (decrease) in cash and cash equivalents	84	179	(123)	(198)	92
Cash and cash equivalents at January 1	12	89	232	232	115
Effect of exchange rate fluctuations on cash held	(7)	(36)	6	5	12
Cash and Cash equivalents at December 31	89	232	115	39	219

SUMMARY SECURITIES NOTE REGISTRATION DOCUMENT

21.5 AIR ICELAND

Operating revenues in 2005 were ISK 3.6 billion, an increase of ISK 626 million from 2003 or 21%. The main reason for this increase is increased demand in air travel, with passenger increase of 18% over the period.

Operating expenses for 2005 were ISK 3.1 billion, an increase of 541 million or 21% from 2003, which can be explained by increase in personnel expenses, both due to increase in operation and increase in salary according to contracts, and cost of fuel due to increased world market prices.

Operating revenues for the first nine months of 2006 were ISK 3.2 billion, an increase of 492 million or 18% from the same period in 2005. This increase can be explained by increasing number of passenger and increasing demand for charter flights with new projects on the west coast of Greenland serviced by the Dash 8 aircraft.

Operating expenses were 2.6 billion for the first nine months of 2006, an increase of 227 million or 10% from the same period in 2005. Two Dash 8 aircraft were introduced and salary cost increased, partly because of training cost. Aircraft lease decreased between years. The company leased all its aircraft from FL Group for 2006, but they have all been bought back, which will result in increase of deprecation and financing cost. Fuel cost has also increased due to increase in world market price.

Total assets of the company amounted to ISK 1,218 million at year end 2005 going from ISK 1,552 million in 2003. In 2004 the company purchased 3 F-50 aircraft for just over ISK 390 million but in 2005 sold those aircraft to the Parent company FL Group and paid off outstanding liabilities for over ISK 400 million.

From 1 January 2006 to 30 September 2006 the company purchased operating assets for ISK 1,687 million including aircraft and real estate form FL Group in the amount of ISK 1,115 million on 1 January 2006. These purchases were primarily financed with new non current liabilities in the amount of ISK 1,503 million. Working capital increases by 54% from year end 2005 to 30 September 2006 and current liabilities increase by 101% over the same period. This increase is mostly due to an increase in operations and the seasonality of the operations, since the third quarter is usually the most profitable.

Equity at year end 2005 is ISK 681 million of which share capital is ISK 420 million. The dividend policy in the Group has been to pay retained earnings to the Parent company.

The cash flow from operating activities reflects a cash generous operation. On regular the company collects money from its customers before service is provided. Cash flows from operating activities at year end 2005 amounted to ISK 282 million. Cash flow from investing activities amounted to ISK 130 million. Cash flow to financing activities amounted to ISK 764 million leaving cash on hand at year end 2005 at ISK 32 million.

Operating cash at 30 September 2006 is ISK 238 million, which is an increase by ISK 102 million from the same period in 2005. Net capital investment is ISK 1,688 million and cash flow from financing activities is ISK 1,750 million due to an increase in liabilities. Cash and cash equivalents increases from year end 2005 until 30 September 2006 increases by ISK 299 million and is ISK 332 million.

Air Iceland paid dividends in April 2003, 2004 and 2005 in the amount of ISK 16 million, 315 million and 355 million respectively.

Table 29. The following table is based on the audited Income Statements of Air Iceland for the years 2003-2005 and for the first nine months of 2006 and the Income Statement for the first nine months of 2005. All figures in ISK million.

	2003 1/1-31/12	2004 1/1-31/12	2005 1/1-31/12	2005 1/1-30/9	2006 1/1-30/9
Operating income:					
Transport revenue	1.972	2.259	2.591	1.885	2.355
Cargo and mail	105	97	103	76	111
Aircraft and air crew lease	408	520	498	415	413
Other operating revenue	438	465	358	337	327
Net operating income:	2.925	3.341	3.551	2.713	3.205
Operating expenses:					
Salaries and other personnel expenses	1.166	1.402	1.573	1.189	1.436
Aircraft fuel	180	230	311	230	289
Aircraft and air crew lease	292	233	281	215.409	91
Aircraft servicing, handling and communication	97	98	98	75	100
Aircraft maintenance expenses	220	199	214	165	151
Other operating expenses	573	560	591	453	489
Net operating expenses:	2.527	2.723	3.068	2.328	2.555
Operating profit before depreciation (EBITDA)	397	618	483	384	650
Depreciation	(132)	(193)	(182)	(137)	(183)
Operating profit before net financial income (EBIT)	265	425	302	248	467
Net financial income (expenses)	(38)	(42)	(55)	(33)	(64)
Profit before tax	227	384	247	214	403
Income tax expense	158	(70)	(46)	(39)	(74)
Profit	385	314	201	176	329

Table 30. The following table is based on Air Iceland's Balance Sheet on 31 December, 2003, 2004 and 2005 and the Balance Sheet at 30 September 2006. All figures in ISK million.

	2003 31/12	2004 31/12	2005 31/12	2006 30/09
Assets:				
Operating assets	557	923	565	2.279
Intangible assets		10	3	1
Long term receivables	19	8		
Tax assets	158			
Investments	22	6	6	6
Total non-current assets	756	946	574	2.286
Inventories	131	94	95	129
Trade receivables	343	334	395	715
Other receivables	118	55	69	94
Intra company receivables				20
Assets for sale			52	
Cash and cash equivalents	205	384	32	332
Total current assets	797	866	644	1.290
Total assets	1.552	1.813	1.218	3.576
Equity:				
Share capital	420	420	420	420
Share reserve	62	77	87	77
Retained Earnings	384	339	175	514
Total equity	866	835	681	1.011
Liabilities:				
Credit institutions	225	304		1.507
Deferred income tax liability		9	21	21
Total non-current liabilities	225	314	21	1.528
Trade and other payables	162	162	171	233
Current maturities of non-current liabilities	66	104		
Tax payables	2	62	31	74
Other payables	175	259	244	363
Prepaid income	48	51	64	111
Intra company payables	9	27	5	256
Total current liabilities	462	664	515	1.037
Total liabilities	687	978	537	2.565
Total equity and liabilities	1.552	1.813	1.218	3.576

Table 31. The following table is based on Air Iceland's audited Cash Flow Statement for the years 2003, 2004 and 2005 and for the first nine months of 2006 and the Cash Flow Statement for the first nine months of 2005. All figures in ISK million.

	2003 1/1-31/12	2004 1/1-31/12	2005 1/1-31/12	2005 1/1-30/9	2006 1/1-30/9
Cash flow from operating activities:					
Profit	385	314	201	176	329
Adjustments for:					
Depreciation	132	193	182	137	183
Profit from sale of assets	(2)	(1)	( )	( )	
Other operating items	(82)	18	14	5	(22)
Working capital from operations	434	524	396	318	491
Net change in operating assets and liabilities	(147)	353	(115)	(181)	(253)
Net cash from operating activities	286	877	282	136	238
Cash flow from investing activities					
Acquisition of operating assets	(355)	(516)	(249)	(171)	(1.687)
Acquisition of intangible assets		(7)			(1)
Proceeds from the sale of assets	2	1	374	373	
Acquisition of shares in other comapnies	(2)		(2)		
Long-term receivables, change	5	5	7	4	
Net cash used in investing activities	(349)	(517)	130	206	(1.688)
Cash flow from financing activities:					
Dividends	(16)	(315)	(355)	(355)	
New long term debt	456	200			1.503
Repayment of borrowings	(310)	(66)	(409)	(380)	
Intra company debt, change				157	247
Net cash used in financing activities	130	(181)	(764)	(578)	1.750
Increase (decrease) in cash and cash equivalents	67	179	(352)	(236)	299
Cash and cash equivalents at January 1	138	205	384	384	32
Cash and Cash equivalents at the end of period	205	384	32	148	332

22 NINE MONTHS REPORT FOR ICELANDAIR GROUP

In this section interim accounts for Icelandair Group for the year 2006 are provided. The interim accounts for the three months ending 31 March 2006 were compiled. The interim accounts for the six months ending 30 June 2006 were reviewed and the interim accounts for the nine months ending 30 September 2006 were audited.

Icelandair, Icelandair Cargo, Loftleiðir Icelandic, Bluebird Cargo and Air Iceland contributed 88% of Icelandair Group's revenues in the first 9 months of 2006. During the same period, these companies contributed 3,404 million of EBIT to Icelandair Group, out of the 3,842 million of EBIT that Icelandair Group had for the period.

During the first nine months of 2005, these companies contributed ISK 1,559 million of EBIT to Icelandair Group compared to ISK 1,475 million for all Icelandair Group´s subsidiaries for the full year 2005 according to the 2005 pro forma accounts. Adjustment to the EBIT in the full year 2005 pro forma accounts for Icelandair Group were 1,116 million, raising the combined EBIT of the subsidiaries comprising Icelandair Group from 1,475 to 2,591. The single largest adjustment is due to lease payments for aircraft made to FL Group in 2005, which are corrected for in the pro forma accounts since Icelandair Group now owns these aircraft. The five subsidiaries thus contributed slightly higher EBIT to Icelandair Group in the first nine months of 2005, than all of Icelandair Group's subsidiaries did in the whole of 2005, according to the 2005 pro forma accounts.

22.1 INTERIM INCOME STATEMENT

Table 32. The income statement for the first, second and third quarters of 2006 and the combined income statement for the first nine months of 2006. All figures in ISK millions.

	Q1 2006 1/1-31/3	Q2 2006 1/4-30/6	Q3 2006 1/7-30/9	2006 1/1-30/9
Operating income:				
Transport revenue	5.555	9.613	12.480	27.648
Aircraft and air crew lease	2.217	2.268	3.290	7.775
Other operating revenue	1.823	2.600	3.707	8.130
Net operating income:	9.595	14.481	19.477	43.553
Operating expenses:				
Salaries and other personnel expenses	3.840	4.447	4.721	13.008
Aircraft fuel	1.654	2.575	3.160	7.389
Aircraft and air crew lease	875	1.253	1.460	3.588
Aircraft servicing, handling and communication	608	1.049	1.290	2.947
Aircraft maintenance expenses	695	808	862	2.365
Other operating expenses	2.188	2.785	3.563	8.536
Net operating expenses:	9.860	12.917	15.056	37.833
Operating profit/(loss) before depreciation (EBITDA)	(265)	1.564	4.421	5.720
Depreciation	(827)	(409)	(642)	(1.878)
Operating profit/(loss) before net financial income (EBIT)	(1.092)	1.155	3.779	3.842
Net financial income	406	347	(747)	6
Share of profit of associates	9	58	24	91
Profit/(loss) before tax	(677)	1.560	3.056	3.939
Income tax expense	122	(281)	(515)	(674)
Profit/(loss) for the period	(555)	1.279	2.541	3.265

22.2 INTERIM BALANCE SHEET

Table 33. The table is based on the audited balance sheet for 30 September 2006. All figures in ISK millions.

	Icelandair Group hf. 30.9.2006
Assets:	
Operating assets	22,684
Intangible assets	15,969
Investments in associates	1,744
Prepaid aircraft acquisitions	11,499
Long-term receivables	2,071
Total non-current assets	53,967
Inventories	1,156
Trade and other receivables	7,793
Cash and cash equivalents	4,976
Total current assets	13,925
Total assets	67,892
Equity:	
Share capital	3,000
Share premium	16,350
Other reserves	767
Retained earnings	3,265
Total equity	23,382
Liabilities:	
Interest bearing loans and borrowings	12,643
Deferred income tax liability	988
Total non-current liabilities	13,631
Interest bearing loans from parent company	4,102
Trade and other payables	11,658
Current maturities of non-current liabilities	11,110
Prepaid income	4,009
Total current liabilities	30,879
Total liabilities	44,510
Total equity and liabilities	67,892

The Company's assets 30 September 2006 are ISK 67,892 million, including ISK 53,967 million in fixed assets. The Company's assets increase by 6% from 1 January 2006. In this period, the Company purchased LatCharter and Airline Services Estonia, which are included in the audited accounts for the nine months ending 30 September 2006. Pre delivery payments (PDP's) because of aircraft purchases decrease by ISK 5,386 million, because of aircraft deliveries during the period. Working capital increased by ISK 3,374 million, mostly due to seasonality.

The Company's liabilities decrease by 1% from year end 2005 until 30 September 2006. The total equity is ISK 23,382 million.

22.3 CASH FLOW

Table 34. Icelandair Group hf.'s cash flow statement for the nine months ended September 30, 2006. All figures in ISK millions.

	2006 1/1-31/3	2006 1/1-30/6	2006 1/1-30/9
Cash flow from operating activities:			
Profit (loss) for the period	(555)	724	3,265
Adjustments for:			
Depreciation	827	1,236	1,878
Other operating items	(692)	(662)	(28)
Working capital from operations	(420)	1,298	5,115
Net change in operating assets and liabilities	1,399	2,559	1,278
Net cash from operating activities	979	3,857	6,393
Cash flow from investing activities			
Acquisition of operating assets	(1,851)	(1,931)	(3,875)
Acquisition of intangible assets	(41)	(67)	(517)
Acquisition of subsidiary, net of cash acquired	5,023	5,023	4,571
Proceeds from the sale of assets	1,746	1,906	1,896
Receivables, change	(1,505)	(276)	(372)
Net cash from investing activities	3,372	4,655	1,703
Cash flow from financing activities:			
Repayment of borrowings	(786)	(1,284)	(1,996)
Repayment of parent company loan	0	0	(1,148)
Net cash used in financing activities	(786)	(1,284)	(3,144)
Decrease in cash and cash equivalents	3,565	7,228	4,952
Effect of exchange rate fluctuations on cash held	65	178	24
Cash and cash equivalents at 31 December	0	0	0
Cash and Cash equivalents at the end of period	3,630	7,406	4,976

In the nine months ending September 30, 2006 net cash provided by operating activities came to ISK 6,393 million, net cash provided by investing activities ISK 1,703 million and net cash used by financing activities amounted to ISK 3,144 million. It should be noted that the cash flow for the Group in 2007 will include repayments of the loans related to the acquisition of Icelandair Group hf.

Operating cash flows for the consolidated company portray a very cash generative operation. The Group has on average negative working capital requirement since the international flight operations receive advance payments but pay costs after the service has been provided. For the period January 1 – September 30 cash flows from operating activities have been relatively stable. Working capital from operations amounted to ISK 5 billion and cash from operating activities amounted to ISK 6 billion. The performance of the Group is very seasonal throughout the year, as most passenger traffic is generated during the summer months making third quarter the best quarter for the company.

Cash flows from investing activities generated ISK 2 billion and repayment of borrowings represented ISK 3 billion leaving cash on hand 5 billion at 30 September 2006.

Icelandair Group had no cash or cash equivalents at 1 January 2006. However, that same day the Company bought all its subsidiaries and acquired the net cash of the subsidiaries, amounting to ISK 5,023 million.

23 2005 PRO FORMA FINANCIAL INFORMATION

Icelandair Group hf. was established in December 2005 and started its operation on 1 January 2006. Its current structure was completed in February 2006 when it finalised taking over the 13 companies, properties, equipments, shares and contracts relating to aircraft trading from FL Group hf. No historical audited accounts therefore exist for Icelandair Group hf. as such for the past years. To give indication on how Icelandair Group hf. would have performed a pro forma income statement has been prepared, for illustrative purposes, for the year 2005. The pro forma income statement is based on the consolidated audited annual reports of the companies that comprise Icelandair Group hf. for the year 2005. All major intra-company transactions have been eliminated from revenue and costs. However, because of its nature, the pro forma financial information addresses a hypothetical situation and, therefore, does not represent the company's actual financial position or results.

23.1 REVIEW OF HISTORICAL FINANCIAL INFORMATION

This section on historical financial information is based on the pro forma consolidated income statement for Icelandair Group hf. for the year 2005.

The pro forma statements are the sum of all audited annual reports of companies comprising Icelandair Group hf., i.e. Icelandair, Icelandair Technical Services (ITS), Icelandair Ground Services (IGS), Icelandair Cargo, Loftleiðir-Icelandic, Bluebird Cargo, Icelandair Hotels, Iceland Travel, Air Iceland, Icelease, IG Invest and Icelandair Shared Services including the following adjustments that were made in order to have the accounts comparable for the year 2005.

Operating assets, aircraft and real estate, that have been purchased from FL Group by the Group, but have historically been leased from FL Group, are assumed to have belonged to the Group in the pro forma accounts to make them comparable and resemble the current structure of the Group.

Intra company business has been estimated and eliminated from both revenue and costs. All the Group's companies were in similar operations over the period.

FL Group hf. had net operating costs that arose because of FL Group hf.'s role as a parent company for the Group companies, those costs have been added on as cost within the Group as it has now taken over as a parent company for these companies.

The operation of Iceland Travel offices in Europe has been eliminated, as the offices were sold at the end of 2005.

On 15 October 2006 Icelandair Group Holding's equity was ISK 27 billion and its share capital was ISK 1 billion.

The pro forma income statement for 2005 is in accordance with IFRS.

SUMMARY

SECURITIES NOTE

REGISTRATION DOCUMENT

23.2 AUDITOR'S REVIEW REPORT

We have reviewed the accompanying pro forma consolidated balance sheet of Icelandair Group hf. as of 1 January 2006 and pro forma consolidated income statement for the year 2005. This consolidated financial information is the responsibility of the Company's management. Our responsibility is to issue a report on this pro forma financial information based on our review.

We have conducted certain procedures which involved comparison to the audited financial statements for the year 2005 for each of the Companies in Icelandair Group hf., consideration of the evidence supporting the necessary adjustments, recalculating the amounts presented in the pro forma balance sheet and income statement based on the information obtained and discussing the pro forma financial information with the directors of Icelandair Group hf. Our review is limited and thus provides less assurance than an audit and accordingly, we do not express an audit opinion.

Based on our review procedures, nothing has come to our attention that causes us not to believe that:
the pro forma financial information has been properly compiled on the basis stated such basis is consistent with the accounting principles used by the Companies in Icelandair Group hf.
the adjustments are appropriate for the purposes of the pro forma financial information as disclosed.
financial information for 2005 is prepared in accordance with IFRS.

We consent to the inclusion of this letter and the reference to our opinion in the Registration Document to be issued by Icelandair Group hf. in the form and context in which it appears.

Reykjavík, 9 February 2007
On behalf of KPMG hf.

Jón Sigurdur Helgason
State authorised public accountant
Icelandic ID No. 050269-3619

Sæmundur Valdimarsson,
State authorised public accountant
Icelandic ID No. 070263-4409

23.3 PRO FORMA INCOME STATEMENT

Table 35. The Company's pro forma Income statement for the year 2005. All figures in ISK millions.

	Scheduled airline operations	Capacity solutions & ac trading	Travel and tourism	Shared services	Total	Adjustment	Pro forma account
OPERATING REVENUE							
Operating revenue							
Passengers	23,007	0	2,592	0	25,599	(50)	25,549
Cargo and mail	3,863	686	103	0	4,652	(753)	3,899
Charter revenue and aircraft lease	6,443	7,814	639	0	14,897	(6,805)	8,092
Other operating revenue	8,330	378	4,199	575	13,481	(5,427)	8,055
	41,643	8,878	7,533	575	58,629	0	45,595
OPERATING COST							
Salaries and related expenses	11,810	655	2,781	315	15,562	(78)	15,483
Aircraft fuel	6,740	265	311	0	7,315	0	7,315
Aircraft lease	6,730	5,882	281	0	12,893	(9,904)	2,989
Aircraft service, handling and communication	3,786	225	98	0	4,110	(519)	3,591
Aircraft maintenace expenses	3,838	248	214	0	4,299	(2,405)	1,894
Booking fees and commission expenses	1,310	0	182	0	1,492	0	1,492
Other operating cost	6,121	500	3,302	61	9,982	(2,105)	7,878
	40,333	7,775	7,169	376	55,653	0	40,642
Operating profit excluding depreciation	1,310	1,103	364	199	2,976	1,977	4,953
Depreciation	892	229	372	9	1,501	861	2,362
Operating profit before financial expence	418	874	(8)	190	1,475	1,116	2,591

23.3.1 REVENUE AND EXPENSES

The Companies largest cost item is salaries and related expense. As a percentage of total operating revenue, salaries are 33.9% in 2005. This cost is primarily related to the workforce in Iceland.

Aircraft fuel has been the single most decisive factor regarding the development of the operational cost base. Aircraft fuel as a percentage of total operating revenue of the Group was 16.0% in 2005. The market price for aircraft fuel has a major impact on overall income. The Company uses effective risk management processes to reduce economic uncertainty and it hedges from 40-80% of fuel purchases 12-18 months in advance.

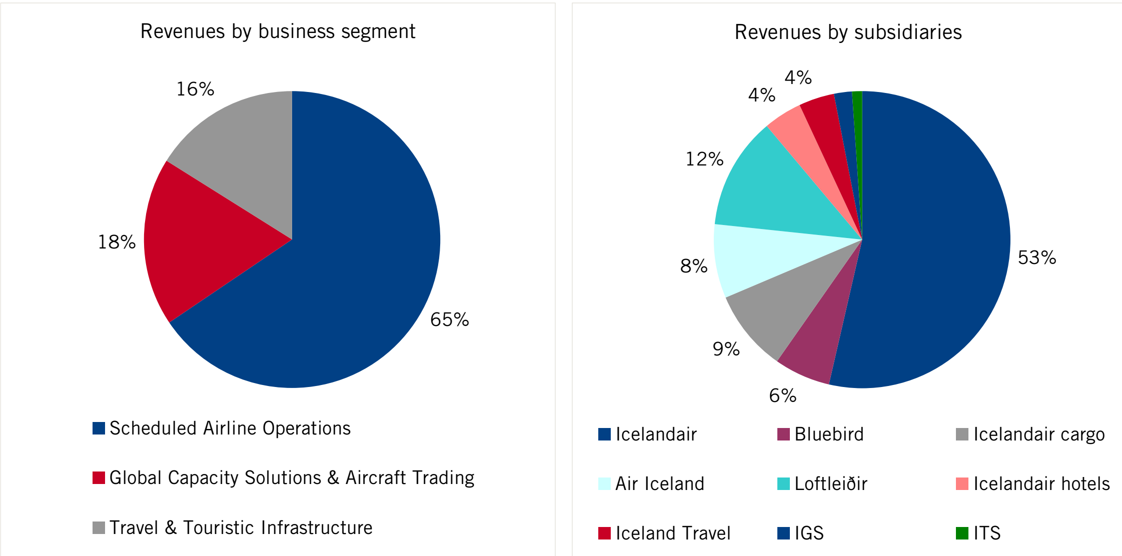
Aircraft leasing expenses have been increasing, mainly due to the fact that in 2005 all new capacity was leased instead of new aircraft being purchased. Another relatively large cost item is airport servicing, which amounted to 7.9% of cost in 2005. That cost item has however been decreasing from 2004 which is mainly due changes in Loftleiðir´s operations. Loftleiðir had more projects in 2005 that did not include "full charter" and the cost of airport services was therefore borne by the customer, instead of Loftleiðir.

As Icelandair Group hf., like most airlines, carries a substantial part of operating assets off balance sheet (operating leases on aircraft), EBITDAR (earnings before interest, taxes, depreciation, amortization and operating leases) is used as an approximate measure of operating cash flows. It is also general practice to use EBITDAR as a benchmark indicator when comparing companies, as this eliminates to a great extent the affects of the decision to purchase or lease operating assets. For Icelandair Group EBITDAR was ISK 7,013 million in 2005 and the EBITDAR margin amounted to 15.4% in 2005. Reasons for changes in the margin are related to increase in fuel cost. In the long run increased fuel unit cost will largely be offset by fuel surcharge (higher unit revenue). The surcharges do not immediately compensate for higher fuel price as airlines have been conservative in adding the surcharge and also because air travel is paid for in advance.

The Group´s earnings before interest and taxes (EBIT) have been rather stable in recent years, despite the volatility in the industry in which the Company operates. The EBIT margin was 5.7% in 2005. The Company has been actively cutting costs and increasing efficiency in its operations to counter rising fuel costs and increased competition. The Company has increased flexibility in its operations and has been able to grow revenue with less investments by better utilisation of assets and the ratio of variable cost has been increasing to make the company capable of expanding or subtracting its operations with respect to market conditions at each time.

The segments share of revenue has remained relatively constant in the period with scheduled airline operations as the largest revenue centre.

Figure 3. Icelandair Group’s revenue by business segment and subsidiaries in 2005



In order to enhance focus the 13 subsidiaries are grouped into three focus areas, Scheduled Airline Operations, Global Capacity Solutions and Aircraft Trading and Travel and Tourism Infrastructure. In addition two subsidiaries play a supporting role. Scheduled airline operations account for 65% of revenue in 2005 and Icelandair accounted for 53% of Icelandair Groups revenue that year.

Scheduled airline operations

Total revenue of the Schedule airline operations segment in 2005 was ISK 29,834 million. Despite an increase in revenue for the past years, EBITDA decreased from 2003 to 2005. The decrease in EBITDA can mainly be explained by the unit costs of Icelandair rising from the year 2003. The reason behind this increase can be traced to increase in fuel prices over the period. Therefore, since 2003, several projects have aimed at reducing the company’s operating expenses to meet higher fuel cost. By reducing sales and administration costs and cost of fleet ownership unit costs have successfully been decreased over the period and if the effect of fuel prices is removed, unit cost actually decreased. Despite the higher fuel price and more competition in the market the Schedule airline operation was profitable for all the years from 2003 to 2005.

Icelandair is the largest subsidiary in the Scheduled airline operations segment accounting for around 77% of EBITDA in 2005. The last few years Icelandair increased the networks capacity by 15% in 2005 and this expansion will continue to pay off in 2006. The last few years have been a period of changes in the operating environment of airlines, both in Europe and North America. Growth in low-fare airlines, on both sides of the Atlantic, has altered the environment for traditional airlines. Icelandair´s environment is no exception, and the company is constantly making efforts to restructure and reduce costs. The primary projects of the company include increasing the share of sales over the Internet, simplifying accounting processes, reducing fuel consumption in flights and continuing to increase the productivity of employees. This gives the company an opportunities to enter into new markets and increase the number of passengers to current destinations.

Global capacity solutions and aircraft trading

Total revenue of the Global capacity solutions and aircraft trading segment was ISK 8,265 million in 2005. EBITDA was ISK 1,103 million in 2005. During the period Loftleiðir-Icelandic advanced into new markets and started to become well known in the international wet-lease market. The company has been taking more profitable projects and gaining new customers. Icelease was founded in the year 2005 as an aircraft trading company and IG Invest as its holding company. The market has been very favourable for last few years and Icelease has been able to take advantage of this market situation. Bluebird Cargo has been a profitable company for some years and it is still doing well.

Travel and Tourism infrastructure

Total revenue of the Travel and Tourism infrastructure segment was ISK 7,343 million in 2005. The companies have gone through some major changes in recent years. Icelandair Hotel opened a modernized Nordica hotel as its flagship and in 2005 Iceland Travel closed all its offices outside Iceland. However, all companies within this segment have performed relatively well for the past years and have taken advantage of the increased numbers of tourists to Iceland.

23.4 PRO FORMA BALANCE SHEET

23.4.1 OPENING PRO FORMA BALANCE SHEET

Icelandair Group hf. was established in its current form on 1 January 2006. At that time, the assets of the Icelandair Group hf's subsidiaries were transformed to Icelandair Group hf. along with fixed assets that have been used in the companies operations but were, in the past, owned by FL Group hf. The following table shows the derivation of the pro forma opening balance sheet of Icelandair Group hf. as on 1 January 2006.

Table 36. Derivation of the Icelandair Group hf. pro forma balance sheet for 1 January 2006 in ISK millions.

	Scheduled airline operations	Capacity solutions & ac trading	Travel and tourism	Shared services	Transfer	Total operations
Assets						
Intangible assets	145	69	107	1	(67)	255
Property and equipment	2,904	1,963	1,389	61	0	6,318
Aircraft purchase prepayments	0	0	0	0	0	0
Interest bearing assets	246	172	131	0	0	550
None interest bearing assets	4,991	898	1,061	111	(923)	6,139
Cash	6,786	837	117	670	0	8,409
Total assets	15,073	3,939	2,805	843	(990)	21,671
Stockholders equity						
Capital stock and other equity	4,391	1,128	125	533	0	6,176
Liabilities						
Interest bearing debt, excl. PDP	1,622	1,974	1,792	0	(923)	4,466
Pre delivery financing of aircraft	0	0	0	0	0	0
None interest bearing liabilities	9,059	837	888	311	(67)	11,028
Total equity and liabilities	15,073	3,939	2,805	843	(990)	21,671

	Asset purchase	Total Subsidiaries	Total parent company	Offset entry	Pro forma account
Assets					
Intangible assets	0	255	0	14,295	14,549
Property and equipment	14,276	20,595	0	0	20,595
Aircraft purchase prepayments	16,886	16,886	0	0	16,886
Interest bearing assets	1,139	1,689	20,471	(20,471)	1,689
None interest bearing assets	8	6,147	0	(614)	5,533
Cash	0	8,409	0	(3,386)	5,023
Total assets	32,309	53,980	20,471	(10,176)	64,274
Stockholders equity					
Capital stock and other equity	0	6,176	19,350	(6,176)	19,350
Liabilities					
Interest bearing debt, excl. PDP	18,364	22,830	1,121	(4,000)	19,951
Pre delivery financing of aircraft	13,890	13,890	0	0	13,890
None interest bearing liabilities	55	11,083	0	0	11,083
Total equity and liabilities	32,309	53,980	20,471	(10,176)	64,274

24 CONSOLIDATED BALANCE SHEET FOR ICELANDAIR GROUP

This section on historical financial information is based on the consolidated balance sheet of Icelandair Group hf. dated 31 October 2006.

In October 2006, Icelandair Group Holding hf. purchased all shares in Icelandair Group hf. from FL Group and acquired at the same time all the shares in Icelandair Group's subsidiaries. On 29 December 2006, the merger of Icelandair Group Holding and Icelandair Group was approved, effective as of 1 November 2006, under the name of Icelandair Group hf. A consolidated balance sheet dated 31 October 2006 for Icelandair Group hf. is derived from the accounts for Icelandair Group hf. and Icelandair Group Holding hf. for the period ending 31 October 2006. The balance sheet is generated internally and has not been audited..

Table 37. Derivation of Icelandair Group hf.'s consolidated balance sheet at 31 October 2006 in ISK millions.

	Icelandair Group hf. 31.10.06	Icelandair Group Holding hf. 31.10.06	Eliminations	Merged company
Assets:				
Operating assets	22,400			22,400
Intangible assets	16,290		10,400	26,690
Investment in subsidiary		33,700	(33,700)	0
Investments in associates	1,750			1,750
Prepaid aircraft acquisitions	11,700			11,700
Long-term receivables	1,815			1,815
Total non-current assets	53,955	33,700	(23,300)	64,355
Inventories	1,200			1,200
Trade and other receivables	6,345			6,345
Cash and cash equivalents	4,300	190		4,490
Total current assets	11,845	190	0	12,035
Total assets	65,800	33,890	(23,300)	76,390
Equity:				
Share capital	1,000	1,000	(1,000)	1,000
Share premium	16,350	25,990	(17,117)	25,223
Other reserves	767	120		887
Retained earnings	5,183	(53)	(5,183)	(53)
Total equity	23,300	27,057	(23,300)	27,057
Liabilities:				
Credit institutions	11,200	6,614		17,814
Deferred income tax liability	1,000			1,000
Total non-current liabilities	12,200	6,614	0	18,814
Credit institutions	3,600			3,600
Trade and other payables	11,100	219		11,319
Current maturities of non-current liabilitie:	12,200			12,200
Prepaid income	3,400			3,400
Total current liabilities	30,300	219	0	30,519
Total liabilities	42,500	6,833	0	49,333
Total equity and liabilities	65,800	33,890	(23,300)	76,390

24.1.1 EQUITY AND LIABILITIES

Total share capital of Icelandair Group hf., including share premium, is ISK 27 billion and long term liabilities after the merger with Icelandair Group Holding hf. are ISK 19 billion compared to Icelandair Group hf.'s ISK 12 billion debt to credit institutions at October 31, 2006. Increase in liabilities and equity is due to the purchase of Icelandair Group hf. by Icelandair Group Holding hf. and results in increased book value of goodwill.

On the balance sheet there are intangible assets amounting to ISK 27 billion. ISK 10.1 billion is due to the purchase of Icelandair Group hf. by Icelandair Group Holding at October 15, 2006, ISK 14.4 billions of intangible assets were created when subsidiaries were transferred from FL Group hf. to Icelandair Group hf.

Operating assets consist mainly of aircraft and buildings. The Group's fleet of aircraft consists of five Boeing 757 used by Icelandair, two Boeing 737 – 300 and two Boeing 737-400 freight aircraft used by Bluebird Cargo, six F-50, two Twin Otter and two Dash 8 all used by Air Iceland.

Around ISK 10 billion of interest bearing debt is due to pre-delivery financing of Boeing 737-800 aircraft and is solely used to finance these aircraft. This debt and assets are only temporarily on the balance sheet as the aircraft will be sold on delivery to third party airlines when delivered from now and until October 2007.

Icelandair Group hf. has an opening cash balance of ISK 4.5 billion.

The balance sheet is strong with an equity ratio of 35% but 40% excluding PDP financing which does not affect the ongoing operations of The Group. Icelandair Group hf. has on average negative working capital requirement since the international flight operations receive advance payments but pay costs after the service has been provided.

24.1.2 FUTURE OUTLOOK

Icelandair Group hf. has set a goal for 5-7% annual internal growth, for the coming years, with hopes of even higher growth for 2006 and 2007. Additionally, the company does not rule out making acquisitions to bolster its operations.

Icelandair Group hf. has an objective to have its EBIT 5-7%, measured against total revenue. EBIT is defined as earnings before interest expense and taxes.

In order to secure the stability of the scheduled operation, Icelandair Group hf. strives to keep a reserve of no less than 10% of Icelandair's ehf. annual revenue. This reserve will be kept in a mix of cash and securities with a maturity less than 90 days. This reserve is estimated to be sufficient to meet a conceivable net cash outflow cased by a sudden shock in Icelandair's ehf. operations.

SUMMARY

SECURITIES NOTE

REGISTRATION DOCUMENT

25 LEGAL AND ARBITRATION PROCEEDINGS

Given the size and the scope of the operations of Icelandair Group and its subsidiaries, there tends to be some type of litigation relating to the Company at any given time. Following is a review of the most significant legal disputes relating to the Company at this time.

25.1 IGS

IGS is preparing a writ to bring a court action to overturn the ruling of the Competition Appellate Committee in Case No. 3/2006, or alternatively to have the fine reduced. The Competition Appellate Committee ordered IGS to pay ISK 60 million in an administrative fine. This fine was imposed because of an abuse of a dominant market position and predatory pricing. The writ has not yet been filed, but is expected to be filed shortly.

25.2 ICELANDAIR

The Icelandic Cabin Crew Association (Flugfreyjufélag Íslands) recently brought a case against Icelandair before the Labour Court regarding two disputes as to the interpretation and performance of the parties' collective bargaining agreement. The action will have negligible, if any, financial consequences for Icelandair.

There is a case pending regarding to Icelandair's operation of its frequent flyer club (Vildarklúbbur Icelandair). Express ferðir ehf. filed the complaint in 2003 and maintains that fidelity rebates are granted by Icelandair through the club and demands that the appropriate sanctions be imposed. It is difficult to predict the consequences if this complaint proves successful, but it seems clear that it would reduce Icelandair's competitiveness and flexibility.

On 16 February 2004 Icelandair's competitor, Express ferðir ehf., submitted a complaint to the Competition Authority. The complainant maintains that Icelandair is in a dominant position and has abused that position by pricing on the routes Copenhagen and London. In May 2006 the Competition Authority submitted its preliminary opinion in the case, stating that it seems that Icelandair has abused its super dominant position by offering flights at a certain price and quantity to Copenhagen and London in 2004. The initial view of the Authority is that this constitutes an abuse of dominant position, a serious breach that can lead to fines being imposed. Following receipt of the Authority's preliminary opinion, Icelandair has submitted its observations and had meetings with the Authority, explaining that the Authority's assumptions are not well founded. It is difficult to predict when a final decision of the Authority can be expected, but it could be in early 2007.

26 CAPITAL RESOURCES

26.1 BORROWING REQUIREMENTS

The company recently finalised the purchase of two 737-400 aircraft in connection with Bluebird Cargo's operations. The purchase price was ISK 2.2 billion and reservations amount to ISK 414 million. ISK 2.1 billion or 80% of this sum will be financed by new debt. Next year two aircraft will be sold to offset this investment. In December 2006 the company signed a letter of intent regarding the purchase of two Boeing 757-200 aircraft, which will, if the purchase will be finalized, result in increased borrowing requirements. Currently there are no other material borrowing requirements. Borrowings as of 30 September 2006 amounted to ISK 51,280 million. Of total borrowings ISK 24,037 million is secured. None of Icelandair Group's borrowing is guaranteed.

26.2 THE FUNDING STRUCTURE

Table 38. The Consolidated assets, equity and liabilities of the Company, based on the Balance Sheet on 1 January and 30 September 2006 and a consolidated balance sheet for Icelandair Group hf. dated 31 October 2006.

	01.01.06	**30.09.06**	**01.11.06**
Total assets	64,280	67,892	76,390
Equity	19,350	23,382	27,057
Long term liabilities	14,861	13,631	18,814
Short term liabilities	30,069	30,879	30,519

The consolidated Balance Sheet for the Company is derived from the accounts for Icelandair Group hf. and Icelandair Group Holding dated 31 October 2006. The accounts, which are internally generated and not audited, take account of the purchase of Icelandair Group hf. on 15 October 2006, when Icelandair Group Holding acquired all the shares in the company from FL Group and the subsequent merger of Icelandair Group and Icelandair Group Holding.

Total share capital of Icelandair Group hf., including share premium, comes to ISK 27 billion and long-term liabilities, after the purchase of Icelandair Group hf. on 15 October 2006, to ISK 19 billion compared to Icelandair Group's ISK 14 billion debt to credit institutions as of 30 September 2006.

The increase in liabilities and equity is due to the purchase of Icelandair Group by Icelandair Group Holding on 15 October 2006 and results in an increased book value of goodwill.

27 SHARE CAPITAL

27.1 ABOUT THE SHARE CAPITAL

The Company was founded on 20 December 2005, under the name Icelandair Group ehf., with a total share capital of ISK 500,000 nominal value. At a shareholders meeting held on 17 February 2006 it was decided to increase the share capital of the Company by ISK 3,500,000 nominal value. After that increment the share capital of the Company was ISK 4,000,000 nominal value. At a shareholders meeting held on 30 May 2006 it was decided to increase the share capital by ISK 2,996,000,000 nominal value. After that increment the share capital of the Company was ISK 3,000,000,000 nominal value. At a shareholders' meeting held on 15 November 2006 it was decided to decrease the share capital by ISK 2,000,000,000 nominal value. Accordingly, the share capital of the Company is ISK 1,000,000,000 nominal value and is divided into equal numbers of shares each having a nominal value of ISK 1.0. All the shares have been fully paid.

At the same shareholders´ meeting the Company was altered from being private limited company to public limited company, in accordance to article 107 of Act no. 138/1994 respecting Private Limited Companies. The name of the Company was changed also, to Icelandair Group hf.

Neither the Company nor its subsidiaries hold any shares in the Company.

27.2 CONVERTIBLE BONDS

On 24 October 2006, Icelandair Group Holding issued bonds in the nominal amount of ISK 2,000,000,000. All rights and obligations attached to the bonds have now been transferred to Icelandair Group hf. The bonds shall carry six-month REIBOR interest with a 3.5% premium for a term of five years; the number of bonds issued shall be at the discretion of the Board, with interest payment dates every six months with the exception that the first interest period shall extend for 15 months, with the option of conversion into shares in the Company at the price of 29.7. The board of directors of the Company are authorised to issue new shares in accordance with the aforesaid authorisation of bondholders and issue new shares to owners of the convertible bonds who exercise their conversion right in accordance with the following rules. The shareholders waive their pre-emptive right in the authorised share offering. The authorisation is permitted for 5 years from 23 November 2006.

In the event that the board of directors exercises the authority granted in Paragraph 2 of Article 4 in the Company's articles of association, the phrasing of the conversion option of the convertible bonds shall be as follows:

(a) The owners of the bonds ("Owners") are entitled to convert the principal of the debt into equity in Icelandair Group ("Issuer"). The conversion option accrues pro rata over the lifetime of the bond, so that an Owner earns the option of converting 20% of the principal of the debt into shares for each passed year of the lifetime of the bond. Thus, the owner will acquire a 20% conversion option on the date ("Option Date") when one year has passed from the issue of the bond, an additional 20% on the date when two years have passed from the issue of the bond etc.

The Owner shall have a conversion option at the price of 29.7 ("Conversion Price"), as adjusted pursuant to subsection (b) below. The number of the shares to which an Owner is entitled shall be determined in accordance with the formula below:

H = HST / BG

where:

H represents the number of shares in the debtor to which an Owner is entitled;

HST represents the principal of the debt under the bond; and

BG represents the Conversion Price, taking into account any adjustments pursuant to subsection (b).

(b) The Conversion Price shall be adjusted as provided below:

(i) If dividends are paid to shareholders during the term of the bond, the Conversion Price shall be reduced in accordance with the following formula:

ABG = BG – (A / H)

where:

ABG represents the adjusted Conversion Price based on the dividend payments;

BG represents the original Conversion Price, as adjusted, if applicable, in accordance with subsection (b) at the time of payment of the dividend;

A represents the total amount of the dividend paid; and

H represents the number of outstanding shares in the Issuer at the time of payment of the dividend.

If a dividend is paid in a medium other than cash, the total amount of the dividend shall be based on the value of the dividend on the day that it is disbursed.

(ii) If the share capital of the debtor is increased through the issue of bonus shares, cf. Chapter V of the Companies Act No. 2/1995, or reduced for the purpose of balancing losses, cf. subsection (1) of paragraph 2 of Article 51 of the Companies Act No. 2/1995, the Conversion Price shall be adjusted in direct proportion to the resulting change in the number of shares in the Issuer.

(iii) In the event that changes are made in the nominal value of each share in the Issuer, the Conversion Price shall be adjusted in direct proportion to the change in the nominal price of the shares.

(c) In the event that the Issuer is dissolved or merged with or taken over by another company so that the operation of the Issuer is continued in another company, Owners shall be notified in writing of such plans. An Owner shall have 14 days from the receipt of such notice to decide whether the debt pursuant to this bond is immediately converted into shares or not. In such an event, the debtor shall be entitled to convert the entire principal of the debt into shares, regardless of the 20% pro rata rule of subsection (a) above. If an Owner decides to convert the debt into shares, the Issuer shall ensure that the debt is converted into shares in the Issuer in such a way that the rights of the Owner in the takeover company or new company are the same as those of other shareholders in the Issuer.

(d) An increase in the share capital of the Issuer pursuant to Chapter V of the Companies Act No. 2/1995, where payment is made for the new shares, shall not have any effect on the conversion option of an Owner, provided that the payment for the shares is not less than 85% of the market price of the Issuer at the time of determining the price of the new shares. If the price of the new shares is lower than the price specified above, the Owner shall be notified of the proposed increase and granted 14 days to convert the debt into shares in order to be able to participate in the increase.

(e) Any other events relating to the Issuer, including the following, shall not affect the conversion option of an Owner:

(i) A reduction in the share capital of the Issuer by a payment to shareholders pursuant to subsection (1) of paragraph 2 of article 51 of the Companies Act No. 2/1995;

(ii) The issue of new convertible bonds pursuant to Chapter VI of the Companies Act No. 2/1995;

(iii) The issue of subscription rights pursuant to Chapter V of the Companies Act No. 2/1995;

(iv) The merger of the Issuer with another company/other companies pursuant to Chapter XIV of the Companies Act No. 2/1995, where the Issuer continues to operate under its current State Registration Number.

(f). An Owner shall exercise his conversion option by sending a notice to such effect to the Issuer during the two-week period preceding an Option Date. An owner may only exercise the entire part of the conversion option earned, and not a part of it. A notice by an Owner shall be regarded as a binding subscription to the shares in question. The Issuer is under obligation to increase his share capital by a number corresponding to the number of shares to which an Owner has an option pursuant to subsection (a) above and deliver the shares to the Owner within 14 days of the Option Date.

(g) When a claim pursuant to this Bond has been converted into a share in the Issuer pursuant to the above, the part of the debt which has been converted shall be regarded as paid in full. A provision for this conversion option has been made in the Articles of Association of the Debtor in accordance with Chapter VI of the Companies Act No 2/1995.

If there will be no dividends paid in the next five years and no share increase, except to meet the requirements of the convertible bonds, then, given that the owners of the bonds will use all their rights to convert bonds to shares, the total number of shares in the Company, at the maturity of the bond, will be 1,067,340,067 and the owners of the bonds will therefore hold 67,340,067 of those shares.

Glitnir banki hf. is the owner of all the convertible bonds described in this subsection.

27.3 STOCK OPTION

The board of directors of the Company is authorised to approve a stock option plan for key employees of the Company and/or its subsidiaries, which entails their permission to buy further specified shares in the Company. For the purpose of fulfilling the said stock option plan, the board of directors of the Company is authorised to increase the company's share capital by up to ISK 60,000,000 – sixty million Icelandic krónur – in nominal value, or up to 6% of the listed shares of the company at any time, which shall be used in fulfilment of the said stock option contracts. The selling price of shares in the Company to holders of stock options shall be decided by the board of directors of the Company at any time; the price shall not be lower than 27 times nominal, but shall in other respects be determined by the average rate of market trading in the company's share ten days prior to the signature of each stock option contract. This authorisation to increase the company's share capital is effective for five years from its approval and may be exercised by the Board in part or in full, at the discretion of the Board. Shareholders' pre-emptive rights pursuant to the Company's Articles of Association do not apply to the increase in share capital pursuant to the above authorisation to the board of directors. In the event that the share capital of the Company is increased during the period of the authorisation beyond ISK 1,000,000,000, the authorisation shall be increased so as to remain always at the level of 6% of the total share capital of the Company at any time. The shares in question are not subject to trading restrictions. The new shares shall carry rights in the company from the date of their listing.

28 ARTICLES OF ASSOCIATION

28.1 OBJECT AND PURPOSE

The object of the Company, according to Article 3 of its Articles of Association, is investment in equity holdings, particularly holdings in other companies engaged in air carrier operations, tourist services and transport operations, buying and selling real estate, credit operations and other related operations.

28.2 BOARD OF DIRECTORS AND MANAGEMENT

The Company's board of directors shall consist of seven members and two alternate members, elected at the Annual General Meeting for a term of one year. Those who intend to stand for election to the board of directors shall inform the Board in writing of their intention at least five days before the Annual General Meeting, or Extraordinary Shareholders' Meeting at which elections are to take place. Only those who have informed the Board of their candidacy are eligible.

The Company's board of directors is the supreme authority in the Company's affairs between shareholders' meetings and shall ensure that the organisation and activities of the Company's operation are generally in correct and good order. The board of directors shall appoint a Managing Director for the Company and decide the terms of his or hers employment. The board of directors and the Managing Director are responsible for the management of the Company. The company's board of directors shall ensure that there is adequate supervision of the company's accounts and the disposal of its assets and shall adopt working procedures in compliance with the Companies Act. Only the board of directors may assign powers of procuration. The signatures of the majority of the members of the Board shall bind the Company.

The board of directors elects a chairman and vice chairman from among its members, and otherwise allocates its obligations among its members as needed. The chairman calls board meetings. A meeting shall also be held if requested by a member of the board of directors or the Managing Director. Meetings of the board are valid if attended by a majority of the members of the board. However, important decisions shall not be taken unless all members of the Board have had the chance to discuss the matter, if possible. The outcome of issues shall be decided by force of vote and in the event of an equality of votes the issue shall be regarded as rejected. The Managing Director attends meetings of the board of directors, even though he or she is not a member of the Board, and has the right to debate and submit proposals unless otherwise decided by the Board in individual cases. A book of minutes shall be kept of proceedings at meetings and shall be signed by participants in the meeting. A board member, or the Managing Director, who is not in agreement with a decision by the board of directors is entitled to have his or her dissenting opinion entered in the book of minutes.

The Managing Director has charge of the day-to-day operations of the company and shall observe the policy and instructions set out by the company's board of directors. Day-to-day operations do not include measures which are unusual or extraordinary Such arrangements can only be made by the Managing Director in accordance with special authority from the Board, unless it is impossible to await the decision of the Board without seriously disadvantaging the operation of the Company. In such instances, the Managing Director shall consult with the chairman, if possible, after which the board of directors shall immediately be notified of the measures. The Managing Director shall ensure that the accounts and finances of the Company conform to the law and accepted practices and that the disposal of the property of the Company is secure. The Managing Director shall provide the Members of the board of directors and Company auditors with any information pertaining to the operation of the Company which they may request, as required by law.

28.3 RIGHTS, PREFERENCES AND RESTRICTIONS OF SHARES

All voting shares carry equal rights and no privileges are attached to shares in the Company. All the shares are freely transferable, unless otherwise provided for by law.

28.4 ACTIONS NECESSARY TO CHANGE SHAREHOLDERS' RIGHTS

According to Article 23 of the Articles of Association the Articles of Association may only be amended at a lawful Annual General Meeting or extraordinary shareholders' meeting, provided that the notice of the meeting clearly indicates that such an amendment is proposed and outlines the main substance of the amendment. A decision is valid only if it has the support of at least 2/3 of the cast votes and the support of shareholders controlling at least 2/3 of the share capital represented at the meeting, provided always that no other force of vote is required by these Articles or statutory law, cf. Article 93 of the Companies Act.

28.5 SHAREHOLDERS' MEETINGS

Shareholders exercise their powers at shareholders' meetings, which hold the company's supreme powers, within the limits provided for in the Articles of Association and law. All shareholders are permitted to attend shareholders' meetings, address them and exercise their voting rights. The auditor of the Company and the Managing Director shall have full rights to address and submit motions at shareholders' meetings even if they are not shareholders. A shareholder may appoint a proxy to attend meetings on his/her behalf, in which case the proxy shall submit a written and dated letter of proxy. Also, shareholders may attend the meeting together with an advisor; the advisor, however, does not have the right to address the meeting, to submit motions or to vote. The board of directors may invite experts to attend individual meetings, if their opinion or assistance is required.

Shareholders' meetings shall be called at the discretion of the board of directors, at the request of the Company auditor , or if shareholders controlling 1/10 of the shares of the Company request a meeting by a written notice. The request shall include a statement to the board of directors explaining the reason for the request, and the board of directors shall notify shareholders of the business on the agenda in the notice of the meeting. When a lawful request for a meeting has been submitted, the board of directors shall call a meeting no later than fourteen days from the time that the request was received. If the board of directors has not called a meeting within that time, shareholders may require a meeting to be called pursuant to the provisions of the Companies Act.

Shareholders' meetings, including the Annual General Meeting, shall be called by a notice to each shareholder by registered mail, telegram or by other verifiable means or, at the discretion of the board of directors, by a notice in the newspapers, with at least one week's notice. A shareholders' meeting is valid, regardless of attendance, if the meeting has been properly convened. Attendance shall be determined based on the number of ballots delivered.

The notice of a shareholders' meeting shall specify the business to be addressed at the meeting. If the agenda includes motions to amend the Articles of the Company, the substance of the motion shall be included in the notice of the meeting. Seven days before a shareholders' meeting, at the latest, an agenda, final submissions and, in the case of annual general meetings, the annual accounts, report of the board of directors and the auditor's report shall be laid open for inspection by shareholders at the Company office.

Each shareholder shall be entitled to have a specific item of business included on the agenda of a shareholders' meeting, provided that such shareholder submits a written request to this effect to the board of directors of the Company with sufficient advance notice for the item to be included on the agenda in accordance with these Articles.

Items of business which are not included on the agenda may not be accepted for final decision at a shareholders' meeting except with the consent of all the shareholders in the Company, but a resolution may be passed to provide guidance to the board of directors of the Company. Lawfully submitted motions for amendments may be put to a vote at the meeting itself, even if they have not been laid open for inspection by shareholders. An Annual General

Meeting is always permitted to conclude matters which it is required to address pursuant to statutory law or the Company Articles.

The Annual General Meeting shall be held before the end of May.

29 ABBREVIATIONS USED IN THIS REGISTRATION DOCUMENT

ACMI	Aircraft Crew Maintenance and Insurance
AOC	Air Operators Certificate
ASE	Airlines Services Estonia
BAA	BAA plc., a British airport company
Bank	Combination of routes via a specific airport at a specific time
CAA	Civil Aviation Authority
CAGR	Compounded Average Growth Rate
Capex	Capital expenditure
CEO	Chief Executive Officer
CFO	Chief Financial Officer
COO	Chief Operating Officer
EBIT	Earnings Before Interest and Taxes
EBITDA	Earnings Before Interest, Taxes, Depreciation and Amortization
EBITDAR	Earnings Before Interest, Taxes, Depreciation, Amortization and Rent
EUR	Euro, the currency of certain European Union member states
FSA	The Financial Supervisory Authority, Iceland
GAAP	Generally Accepted Accounting Principles
GSA	General Sales Agent
Hub	An airport serving as a connection point in a route network
ICEX	Iceland Stock Exchange
IFRS	International Financial Reporting Standards
IGS	Icelandair Ground Service
ISD	Icelandic Securities Depository
ISK	Icelandic króna, the currency of Iceland
ITB	Icelandic Tourist Board
ITS	Icelandair Technical Service
MD	Managing Director
MICE	Meetings Incentives Conference Events
PAYE	Pay-As-You-Earn
PDP	Pre Delivery Payment
Q1, Q2, Q3, Q4	Different quarters of the year
The Companies Act	Act No. 2/1995 on Public Limited Companies
The Securities Act	Act No. 33/2003 on Securities Transactions
USD	United States Dollar
VP	Vice President

30 APPENDICES

30.1 ICELANDAIR GROUP HF.'S ARTICLES OF ASSOCIATION

30.2 STOCK OPTION PLAN FOR KEY EMPLOYEES

30.3 THE CONSOLIDATED BALANCE SHEET FOR ICELANDAIR GROUP HF. DATED 31 OCTOBER 2006. THE BALANCE SHEET IS INTERNALLY GENERATED AND HAS NOT BEEN AUDITED.

30 APPENDICES

30.1 ICELANDAIR GROUP HF.'S ARTICLES OF ASSOCIATION

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ARTICLES OF ASSOCIATION

OF

ICELANDAIR GROUP HF.

Chapter I

Company Name, Domicile and Object

Article 1

The Company is a limited liability company. The name of the Company is **Icelandair Group hf.**

Article 2

The domicile of the Company is at Reykjavíkurflugvöllur, 101 Reykjavík.

Article 3

The object of the company is investment in equity holdings, particularly holdings in other companies engaged in air carrier operations, tourist services and transport operations, buying and selling real estate, credit operations and other related operations.

Chapter II

Share Capital of the Company

Article 4

The share capital of the Company is ISK 1,000,000,000 – one billion Icelandic krónur. Each share in the Company corresponds to one Icelandic króna or multiples thereof.

The Board of Directors of the Company is authorised to issue bonds in the amount of ISK 2,000,000,000, which shall carry six-month REIBOR interest with a 3.5% premium for a term of five years; the number of bonds issued shall be at the discretion of the Board, with interest payment dates every six months with the exception that the first interest period shall extend for 15 months, with the option of conversion into shares in the Company at the price of 29.7. The Board of Directors of the Company are authorised to issue new shares in accordance with the aforesaid authorisation of bondholders and issue new shares to owners of the convertible bonds who exercise their conversion right in accordance with the following rules. The shareholders waive their pre-emptive right in the authorised share offering. The authorisation is permitted for 5 years from 23 November 2006.

The Board of Directors of the Company is authorised to approve a stock option plan for the key employees of the company and/or its subsidiaries, which entails their permission to buy further specified shares in the company. For the purpose of fulfilling the said stock option plan, the Board of Directors of the Company is authorised to increase the company's share capital by up to ISK 60,000,000 – sixty million Icelandic krónur – in nominal value, or up to 6% of the listed shares of the company at any time, which shall be used in fulfilment of the said stock option contracts. The selling price of shares in the Company to holders of stock options shall be decided by the Board of Directors of the Company at any time; the price shall not be lower than 27 times nominal, but shall in other respects be determined by the average rate of market trading in the company's share ten days prior to the signature of each stock option contract. This authorisation to increase the company's share capital is effective for five years from its approval and may be exercised by the Board in part or in full, at the discretion of the Board. Shareholders' pre-emptive rights pursuant to the Company's Articles of Association do not apply to the increase in share capital pursuant to the above authorisation to the Board of Directors. In the event that the share capital of the Company is increased during the period of the authorisation beyond ISK 1,000,000,000, the authorisation shall be increased so as to remain always at the level of 6% of the total share capital of the Company at any time. The shares in question are not subject to trading restrictions. The new shares shall carry rights in the company from the date of their listing.

In the event that the Board of Directors exercises the authority granted in Paragraph 2 of this Article 4, the phrasing of the conversion option of the convertible bonds shall be as follows:

(a) The owners of the bonds ("Owners") are entitled to convert the principal of the debt into equity in Icelandair Group ("Issuer"). The conversion option accrues pro rata over the lifetime of the bond, so that an Owner earns the option of converting 20% of the principal of the debt into shares for each passed year of the lifetime of the bond. Thus, the owner will acquire a 20% conversion option on the date ("Option Date") when one year has passed from the issue of the bond, an additional 20% on the date when two years have passed from the issue of the bond etc.

The Owner shall have a conversion option at the price of 29.7 ("Conversion Price"), as adjusted pursuant to subsection (b) below. The number of the shares to which an Owner is entitled shall be determined in accordance with the formula below:

$H = HST / BG$

where:

H represents the number of shares in the debtor to which an Owner is entitled;

HST represents the principal of the debt under the bond; and

BG represents the Conversion Price, taking into account any adjustments pursuant to subsection (b).

(b) The Conversion Price shall be adjusted as provided below:

(i) If dividends are paid to shareholders during the term of the bond, the Conversion Price shall be reduced in accordance with the following formula:

$$ABG = BG - (A / H)$$

where:

ABG represents the adjusted Conversion Price based on the dividend payments;

BG represents the original Conversion Price, as adjusted, if applicable, in accordance with subsection (b) at the time of payment of the dividend;

A represents the total amount of the dividend paid; and

H represents the number of outstanding shares in the Issuer at the time of payment of the dividend.

If a dividend is paid in a medium other than cash, the total amount of the dividend shall be based on the value of the dividend on the day that it is disbursed.

(ii) If the share capital of the debtor is increased through the issue of bonus shares, cf. Chapter V of the Companies Act No. 2/1995, or reduced for the purpose of balancing losses, cf. subsection (1) of paragraph 2 of Article 51 of the Companies Act No. 2/1995, the Conversion Price shall be adjusted in direct proportion to the resulting change in the number of shares in the Issuer.

(iii) In the event that changes are made in the nominal value of each share in the Issuer, the Conversion Price shall be adjusted in direct proportion to the change in the nominal price of the shares.

(c) In the event that the Issuer is dissolved or merged with or taken over by another company so that the operation of the Issuer is continued in another company, Owners shall be notified in writing of such plans. An Owner shall have 14 days from the receipt of such notice to decide whether the debt pursuant to this bond is immediately converted into shares or not. In such an event, the debtor shall be entitled to convert the entire principal of the debt into shares, regardless of the 20% pro rata rule of subsection (a) above. If an Owner decides to convert the debt into shares, the Issuer shall ensure that the debt is converted into shares in the Issuer in such a way that the rights of the Owner in the takeover company or new company are the same as those of other shareholders in the Issuer.

(d) An increase in the share capital of the Issuer pursuant to Chapter V of the Companies Act No. 2/1995, where payment is made for the new shares, shall not have any effect on the conversion option of an Owner, provided that the payment for the shares is not less than 85% of the market price of the Issuer at the time of determining the price of the new shares. If the price of the new shares is lower than the price specified above, the Owner shall be notified of the proposed increase and granted 14 days to convert the debt into shares in order to be able to participate in the increase.

(e) Any other events relating to the Issuer, including the following, shall not affect the conversion option of an Owner:

(i) A reduction in the share capital of the Issuer by a payment to shareholders pursuant to subsection (1) of paragraph 2 of article 51 of the Companies Act No. 2/1995;

(ii) The issue of new convertible bonds pursuant to Chapter VI of the Companies Act No. 2/1995;

(iii) The issue of subscription rights pursuant to Chapter V of the Companies Act No. 2/1995;

(iv) The merger of the Issuer with another company/other companies pursuant to Chapter XIV of the Companies Act No. 2/1995, where the Issuer continues to operate under its current State Registration Number.

(f). An Owner shall exercise his conversion option by sending a notice to such effect to the Issuer during the two-week period preceding an Option Date. An owner may only exercise the entire part of the conversion option earned, and not a part of it. A notice by an Owner shall be regarded as a binding subscription to the shares in question. The Issuer is under obligation to increase his share capital by a number corresponding to the number of shares to which an Owner has an option pursuant to subsection (a) above and deliver the shares to the Owner within 14 days of the Option Date.

(g) When a claim pursuant to this Bond has been converted into a share in the Issuer pursuant to the above, the part of the debt which has been converted shall be regarded as paid in full. A provision for this conversion option has been made in the Articles of Association of the Debtor in accordance with Chapter VI of the Companies Act No 2/1995.

Article 5

The share capital of the Company may be increased, either by subscription to new shares or the issue of bonus shares, by a resolution of a shareholders' meeting, both requiring the same force of vote as amendments to these Articles of Association. Shareholders have pre-emptive rights to new shares in proportion to their holdings in the Company and within the time limits specified in the decision to increase the Company share capital. In the event that any shareholder does not exercise his or her pre-emptive rights in full, other shareholders shall be entitled to increased their subscription rights. A shareholders' meeting may, by a 2/3 majority vote, decide to waive pre-emptive rights on increases in share capital, provided that there is no discrimination.

In the event that a shareholder has not paid in the required share capital by the due date, he or she shall pay penalty interest on the amount due from that date to the date of payment, in addition to costs incurred for the collection of the payment. Other means of dealing with defaults may also be used, as provided for by law at any time.

Only a shareholders' meeting can decide on a reduction in share capital.

All shares carry equal rights.

Article 6

Shares in the Company are issued electronically pursuant to the provisions of the Act on the Electronic Registration of Title to Securities.

The Board of Directors shall maintain a register of shares in a lawful form. Registry of title in a securities depository constitutes full proof of title to shares in the Company and adequate basis for entry in the register of shares.

The register of shares shall be preserved in the office of the Company, where all shareholders shall have access to it and permission to inspect its contents.

Article 7

Shares in the Company may be pledged or sold without restriction except as otherwise provided by law.

The sale of shares to foreign nationals is subject to the provisions of Icelandic statutory law, as current at any time.

Transfers of title to shares, whether by sale, gift, inheritance, the settlement of an estate or attachment, shall be promptly notified to the Company's office and the Company's register of shares shall then be amended accordingly.

Parties who have acquired shares in the Company cannot exercise their rights as shareholders until their names have been entered in the register of shares, or if they have given due notice and submitted proof of title.

For the Company, the register of shares shall be regarded as full proof of title to any shares in the Company, and dividends at any time, as well as all notices, shall be sent to the party registered at any time as the owner of the shares in question in the Company's register of shares. The Company is not liable for the loss of any payments or notices resulting from neglect by shareholders to notify changes in title or address.

Article 8

No privileges are attached to shares in the Company.

Shareholders shall not be required to suffer redemption of their shares except as provided by law.

Article 9

The Company shall not grant loans against its own shares in the Company except as permitted by statutory law. The Company may acquire its own shares to the extent permitted by statutory law. Voting rights of shares owned by the Company in itself may not be exercised.

The Company shall not grant loans to shareholders, Board members, the Managing Director or senior officers of the Company, nor provide them with guarantees. The provisions of this Article do not, however, apply to normal business loans or purchases by the Company's employees, or an associated company, of shares, or the purchase of shares for their benefit, as permitted by law.

Article 10

Shareholders are under obligation, without specific undertaking, to observe the Articles of Association of the Company in their current form or as lawfully amended at any time. Shareholders can not be obligated, neither by the Articles of the Company nor by amendments thereto, to increase their shareholding.

Shareholders are not liable for the commitments of the Company beyond their share in the Company unless they assume such further commitments under a separate legal instrument. This provision cannot be amended by any resolution of a shareholders’ meeting.

Chapter III

Shareholders' Meetings

Article 11

The supreme authority in the affairs of the Company is entrusted to lawful shareholders’ meetings, within the limits set by these Articles of Association and statutory law.

Shareholders exercise their powers of decision at shareholders’ meetings.

All shareholders may attend and speak at shareholders’ meetings and exercise their right to vote.

A shareholder may appoint a proxy to attend meetings on his/her behalf. The proxy shall submit a written and dated letter of proxy.

A shareholder may attend a meeting accompanied by an advisor. The advisor shall not be entitled to speak, submit motions or vote at shareholders’ meetings.

The auditor of the Company and the Managing Director shall have full rights to speak and submit motions at shareholders’ meetings even if they are not shareholders

The Board of Directors may invite experts to attend individual meetings, if their opinion or assistance is required.

Article 12

Shareholders’ meetings shall be called at the discretion of the Board of Directors, at the request of the Company auditor , or if shareholders controlling 1/10 of the shares of the Company request a meeting by a written notice. The request shall include a statement to the Board of Directors explaining the reason for the request, and the Board of Directors shall notify shareholders of the business on the agenda in the notice of the meeting.

When a lawful request for a meeting has been submitted, the Board of Directors shall call a meeting no later than fourteen days from the time that the request was received. If the Board of Directors has not called a meeting within that time, shareholders may require a meeting to be called pursuant to the provisions of the Companies Act.

Article 13

Shareholders' meetings, including the Annual General Meeting, shall be called by a notice to each shareholder by registered mail, telegram or by other verifiable means or, at the discretion of the Board of Directors, by a notice in the newspapers, with at least one week's notice. A shareholders' meeting is valid, regardless of attendance, if the meeting has been properly convened. Attendance shall be determined based on the number of ballots delivered.

The notice of a shareholders' meeting shall specify the business to be addressed at the meeting. If the agenda includes motions to amend the Articles of the Company, the substance of the motion shall be included in the notice of the meeting. Seven days before a shareholders' meeting, at the latest, an agenda, final submissions and, in the case of annual general meetings, the annual accounts, report of the Board of Directors and the auditor's report shall be laid open for inspection by shareholders at the Company office.

Each shareholder shall be entitled to have a specific item of business included on the agenda of a shareholders' meeting, provided that such shareholder submits a written request to this effect to the Board of Directors of the Company with sufficient advance notice for the item to be included on the agenda in accordance with these Articles.

Items of business which are not included on the agenda may not be accepted for final decision at a shareholders' meeting except with the consent of all the shareholders in the Company, but a resolution may be passed to provide guidance to the Board of Directors of the Company. Lawfully submitted motions for amendments may be put to a vote at the meeting itself, even if they have not been laid open for inspection by shareholders. An Annual General Meeting is always permitted to conclude matters which it is required to address pursuant to statutory law or the Company Articles.

Article 14

The Annual General Meeting shall be held before the end of the month of May each year.

The agenda of the Annual General Meeting shall include the following items of business:

1. The Board of Directors of the Company shall report on the Company's position and its activities in the preceding year of operation
2. Audited annual accounts shall be submitted for approval
3. Decisions shall be taken concerning the disposal of the profit or loss of the Company during the fiscal year

4. Motions to amend the Articles of the Company shall be addressed, if submitted;
5. A decision shall be made on the remuneration of the Board of Directors
6. A Board of Directors shall be elected
7. Company auditors shall be elected
8. Discussions and voting on other items of business lawfully submitted at the meeting.

Article 15

The Chairman of the Board of the Company, or an elected chairman of the meeting, shall preside over shareholders' meetings and the election of a secretary. At the outset of the meeting the chairman of the meeting shall verify whether the meeting was properly called and declare whether such is the case. The chairman of the meeting presides over discussions and voting.

Article 16

Each share of one króna shall carry one vote.

All ordinary business at shareholders' meetings shall be decided by majority vote, except as otherwise provided in these Articles of Association or by law. In the event of an equality of votes at elections to posts in the Company, the election shall be decided by casting lots.

Article 17

A brief account of proceedings at shareholders' meetings shall be entered in a book of minutes, together with all resolutions of the meeting and results of voting. These minutes shall constitute conclusive proof of proceedings at shareholders' meetings.

Chapter IV

The Board of Directors of the Company etc.

Article 18

The Board of Directors of the Company shall be composed of seven members and two alternate members elected at the Annual General Meeting for a term of one year. The eligibility of members of the Board is subject to statutory law. Elections to the Board shall always be by ballot if the number of nominations exceeds the number of Members to be elected.

Prospective candidates to the Board of Directors shall submit a written notice to such effect to the Board of Directors no later than five days before the start of the Annual General Meeting, or extraordinary shareholder's meeting where elections to the Board of Directors are included on the agenda. Only those who have submitted a notice pursuant to the above are eligible as candidates at an Annual General Meeting.

At the Annual General Meeting elections to the Board of Directors shall be restricted to ballots with the names of candidates who announced their candidature within the set deadline.

Article 19

The Board of Directors holds the supreme authority in the affairs of the Company between shareholders' meetings and is responsible for ensuring that its organisation and operation are at all times in correct and proper order.

The Board of Directors shall appoint a Managing Director for the Company and decide the terms of his or her employment. The Board of Directors of the Company and the Managing Director are responsible for the management of the Company.

The Board of Directors shall ensure adequate supervision of the accounts of the Company and the disposal of its assets.

The Board of Directors shall establish working procedures in compliance with the provisions of the Companies Act.

Only the Board of Directors may assign powers of procuration.

The signatures of the majority of the Board shall bind the Company.

Article 20

The Board of Directors of the Company shall elect a Chairman of the Board and Vice-Chairman from among its members, and allocate tasks among themselves in other respects as required.

The Chairman shall call Board meetings and ensure that all the members of the Board are notified of such meetings. Meetings of the Board shall be held at the discretion of the Chairman. The Chairman shall also call a meeting of the Board if requested by one member of the Board or the Managing Director. Meetings of the Board of Directors are valid if attended by a majority of the members of the Board. However, no important decision shall be taken unless all members of the Board have had an opportunity to discuss the matter, if possible. The outcome of issues shall be decided by force of vote. In the event of an equality of votes the issue shall be regarded as rejected.

The Managing Director shall attend Board meetings even if he or she is not a member of the Board, and shall have the right to participate in discussions and submit proposals, unless otherwise decided by the Board in individual cases.

A book of minutes shall be kept of proceedings at meetings of the Board of Directors, signed by the participants in the meeting. A member of the Board of Directors or Managing Director who disagrees with a Board decision is entitled to have his or her dissenting opinion recorded in the minutes.

Article 21

The Managing Director of the Company and the Board of Directors are jointly responsible for the management of the Company.

The Managing Director has charge of the day-to-day operation of the Company, and in this respect he or she shall observe the policy and instructions of the Board of Directors. Day-to-day operations do not include measures which are unusual or extraordinary. Such measures may only be taken by the Managing Director pursuant to special authorisation from the Board of Directors of the Company unless it is impossible to wait for the decisions of the Board of Directors without seriously disadvantaging the operation of the Company. In such an event, the Managing Director shall consult with the Chairman of the Board, if possible, after which the Board of Directors shall immediately be notified of the measures.

The Managing Director shall ensure that the accounts and finances of the Company conform to the law and accepted practices and that the disposal of the property of the Company is secure.

The Managing Director shall provide the Members of the Board of Directors and Company auditors with any information pertaining to the operation of the Company which they may request, as required by law.

Chapter V

Accounts, Auditing etc.

Article 22

At the Annual General Meeting of the Company a chartered auditor or auditing firm shall be elected for the Company for a term of one year to review the accounts of the Company and submit the conclusions of the review to the Annual General Meeting. The auditor shall have access to all books and documents of the Company for such purpose. Auditors shall not be elected from among the members of the Board or employees of the Company. The qualifications and eligibility of auditors at elections are in other respects governed by law.

The operating year and financial year of the Company shall be the calendar year. The Board of Directors shall have prepared the annual accounts of the Company and submitted them to the Company's auditors no later than one month before the Annual General Meeting.

Part VI

Amendment of the Articles, Dissolution of the Company etc.

Article 23

These Articles of Association may only be amended at a lawful Annual General Meeting or extraordinary shareholders' meeting, provided that the notice of the meeting clearly indicates that such an amendment is proposed and outlines the main substance of the amendment. A decision is valid only if it has the support of at least 2/3 of the cast votes and the support of shareholders controlling at least 2/3 of the share capital represented at the meeting, provided always that no other force of vote is required by these Articles or statutory law, cf. Article 93 of the Companies Act.

Article 24

The dissolution of the Company, its division or merger with other companies is subject to the provisions of statutory law concerning limited liability companies.

Article 25

Matters on which these Articles provide no guidance shall be governed by the provisions of the Companies Act and such provisions of other current statutory law as may be applicable.

So approved at a shareholders' meeting on 28 December 2006.

On the Board of Directors of Icelandair Group hf.

Finnur Ingólfsson

30.2 STOCK OPTION PLAN FOR KEY EMPLOYEES

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Icelandair Group hf.

Stock Option Plan for Key Employees

Stock Option Plan for Key Employees
of Icelandair Group hf.

1. Purpose

The purpose of this Stock Option Plan is to enable Icelandair Group hf. (hereinafter referred to as “the Company”) to attract and retain employees, both in the Company itself and its subsidiaries, through an attractive system of remuneration, particularly as regards the key personnel in the management and technological development of the Company, and at the same time provide such employees with an opportunity to acquire a share in the Company and thereby contribute to increased incentives and reward for promoting the increased growth and prosperity of the Company in the long term. Accordingly, the Plan provides for the granting of options to employees by the means most suitable for each employee participating in the Stock Option Plan. Any reference to the Company below may therefore apply to Icelandair Group hf. or its subsidiaries.

2. Stock Option and Legal Position of Employee

Stock option in this Plan refers to the option of an employee of the Company and/or its subsidiaries to acquire a share in the Company at a set time, or over a set period, at a predetermined price, provided that the employee meets certain conditions regarding employment for the Company.

This option is an independent right based on separate contracts with individual employees. This option is not connected with the employment terms of the employee or his/her contracts with the Company or its subsidiaries in other respects than provided for in this Plan and the Stock Option Contract entered into with the employee.

3. Effective Date and Effective Term of the Plan

This Plan will take effect on 29 December 2006 and remain in effect while the authorisation granted to the Board of Directors at the shareholders’ meeting held on 29 December 2006 remains effective without change.

Stock options granted to employees which have not been exercised shall in any case lapse four weeks after the annual general meeting of the company in 2010.

4. Implementation and Supervision

This Plan and its implementation falls under the authority and supervision of the Wage Terms Committee of the Company pursuant to authorisation granted by the Board of Directors of the Company. The Wage Terms Committee has the power of decision in all matters requiring decision pursuant to the Plan, unless other parties are specifically designated as responsible for decisions on specific issues.

The Wage Terms Committee will decide the stock option of the Managing Director of the Company under this Stock Option Plan, after which the Wage Terms Committee, on the recommendation of the Managing Director, will decide which employees of the Company and/or its subsidiaries qualify for stock options and thereby participation in the Stock Option Plan and when stock options should be granted pursuant to contracts with individual participants. Furthermore, the Wage Terms Committee shall decide on the specific terms of Stock Option Contracts.

Relations with stock option holders, supervision of the preparation of Stock Option Contracts and comparable arrangements shall be undertaken by the Wage Terms Committee and/or the Managing Director of the Company, as approved by the Wage Terms Committee at any time, e.g. as regards amount and price of shares. The Managing Director shall submit proposals to the Wage Terms Committee on the number and price of shares to individual employees. The Wage Terms Committee is responsible for relations with the Managing Director as regards any stock option of the Managing Director.

5. Amount of Stock Options and Procurement of Shares

The authorisation of the Board of Directors to issue stock options is limited so that the outstanding options at any time must never amount to a higher proportion than 6% of the total shares in the Company at any time, currently shares in the nominal amount of ISK 60,000,000. The amount of the stock option of any single employee shall not exceed 10% of the total issued stock options. However, this rule shall not apply to the Managing Director of the Company.

The Company can both use its own shares for options, purchase shares, or issue new shares as authorised by a shareholders' meeting, in order to meet Company obligations pursuant to Stock Option Contracts. If the Company is unable to obtain shares for this purpose, the Board of Directors of the Company is authorised to pay to the holders of the options a fair market price in cash for an exercised option. In the event that the Company is at such time listed in a stock market, the fair market price shall be the closing price of shares in the Company in the stock market on the date that a participant in the Stock Option Plan announces to the Company his/her desire to exercise his/her option. In the event that the Company is unlisted at such date and the parties cannot agree on a market price, the value of the stock option shall be determined by two assessors appointed by the District Court of Reykjavík. Their appraisal of the value of the stock option shall be final. The cost of the appraisal shall be paid by the Company, unless its offer was equal to or higher than the appraisal, in which case the cost shall be divided equally between the parties.

6. Participants – Stock Option Holders

All the permanently employed employees of the Company and/or its subsidiaries who are defined as key employees pursuant to the recommendation of the Managing Director, as approved by the Wage Terms Committee, qualify as stock option holders pursuant to this Stock Option Plan.

Furthermore, other parties with close relations to the Company's operations can also qualify as participants in this Stock Option Plan, e.g. consultants or other contractors of the Company.

7. Rules Governing Stock Options on Termination of Employment and Decease of Holders

In the event of the resignation of an employee, any earned and unexercised option shall lapse on the date that he/she resigns from the Company. In the event that the employee is dismissed without notice on the grounds of gross default of his/her employment contract which justifies immediate dismissal, all of his/her options gained shall be cancelled on the same day that he/she is dismissed. If an employee is dismissed with contractual notice without fault, the Managing Director and/or Wage Terms Committee will determine the disposal of any earned stock option in that year, and all rights shall lapse at the end of that year.

If an employee becomes incapable of work as a result of permanent disability the employee will retain his/her right during the year in which the disability occurred, but all options shall lapse after the end of that year.

If an employee retires at retirement age the employee will retain his/her right during the year in which the retirement occurred, but all options shall lapse after the end of that year.

On the decease of an employee, the estate of the employee shall retain the rights relating to earned options during the year that the decease occurred, but all options shall lapse after the end of that year.

"Unexercised earned option" shall mean the right earned by an employee to purchase shares up until the time he/she ceases to work for the Company. The stock option exercisable by an employee following such time as termination of employment takes place shall in any event lapse at the time of termination of employment.

The Wage Terms Committee is authorised to negotiate deviations from the provisions of this Article in special circumstances.

8. Stock Options

On the delivery of stock options to employees, the Company shall enter into a written Stock Option Contract with the employee. The option shall not be regarded as having been delivered, nor shall it become exercisable, until such time as a Stock Option Contract has been concluded with the employee in question. In this context, the date of the Stock Option Contract shall be regarded as the date of delivery of the stock option.

The Stock Option Contract shall contain the terms and conditions established by the Wage Terms Committee of the Company regarding redemption date(s), i.e. the date(s) on which an employee may exercise, in part or in full, his/her option to acquire shares. The Contract shall also contain provisions on a final date, i.e. the final date on which an employee can exercise his/her option and the amount of shares that the holder of the option may acquire at any time. The terms and conditions of Stock Option Contracts need not be uniform, and options may be adapted to the needs of individual employees. E.g., the amount of an option may be linked to the income of the Company or the contribution margin of specific employees.

9. Amendments to Employee Stock Options

Stock options, earned and unearned, are subject to change by the Wage Terms Committee of the Company, e.g. as regards the amount of the option and maximum amounts, e.g. as a result of the issue of bonus shares, restructurings, issue of subscription rights, issue of convertible bonds, increases and decreases in share capital, mergers, demergers, take-overs or other changes which may affect the value of the options. However, in the implementation of such changes, care shall be taken to ensure that the value of the stock option remains largely unchanged in spite of any changes.

Stock options shall not in any way curtail the authority of the Wage Terms Committee or the Board of Directors of the Company or shareholders' meetings to make any necessary changes in the operation of the Company, e.g. through borrowings, sales of assets or other restructuring in the operation of the Company.

In the event that an obligation arises to pay such taxes the employee shall be entirely liable to the company and/or its subsidiaries for their payment. If the company and/or subsidiares are required to pay such taxes a corresponding claim shall ensue for reimbursement by the employee.

The Wage Terms Committee may at any time submit a recommendation to the Board of Directors to change, improve or terminate the Stock Option Plan, in full or in part. Furthermore, the Wage Terms Committee and Board of Directors of the Company is authorised to change and adapt the Stock Option Plan to any tax law amendments which may be made regarding stock options. However, the Wage Terms Committee and Board of Directors may not alter earned stock options for the above reasons unless the alteration is to the advantage of the holder of the stock option.

10. Tax Obligations

The Company is not responsible for any tax consequences which may result from the participation by employees in the Stock Option Plan except to the extent of withholding employees' withholding tax and any other taxes which the Company is required to account for in relation to wage payments at any time.

According to statutory law, as current at the time of conclusion of this Contract, the difference between the purchase price pursuant to the Contract and the market price of shares in the Company constitutes taxable income of the employee. The Company may be responsible for the payment of taxes relating to any Stock Option Contract concluded on the basis of this Stock Option Plan. The employee shall undertake, at the time of paying the stock option price, to deliver to the Company an amount corresponding to the tax imposed on the employee in respect of the stock option, and the Company shall in such an event pay the employee's attendant income tax. Notwithstanding the fact that the income is defined as earned income this does not mean that the employee has a corresponding right to a pension contribution by the Company, nor to vacation rights.

The employee shall himself/herself declare and pay any capital gains tax on his/her profit from the sale of the shares covered by any option pursuant to this Stock Option Plan as required by law at any time.

11. Assignment of a Stock Option

Any stock option obtained by an employee pursuant to a Stock Option Contract is for the employee's personal benefit and cannot be assigned to any third party, except as specifically approved by the Wage Terms Committee, subject to the special provisions relating to the decease of the stock option holder.

12. Insider Trading

The employee should be informed that he/she is an insider of the Company in the understanding of the Act on Securities Undertakings. Employees shall undertake to exercise their options pursuant to this Stock Option Plan so as to avoid any violation of statutory law concerning insider trading.

In the event that it proves impossible for an employee to exercise his/her option on a proposed redemption date owing to the fact that insider information is available within the Company, the redemption date in question shall be postponed and the employee shall then be permitted to redeem the number of shares specified in the redemption notice as soon as possible in compliance with statutory law.

13. Resolutions of Disputes and Confidentiality

In the event of any dispute concerning the interpretation of the Stock Option Plan or individual Stock Option Contracts based on the Plan, either party may, without obligation, submit the dispute to arbitration. Each party shall nominate one member to the arbitration tribunal and seek a consensus on a third member who shall act as chairman of the arbitration tribunal. In the event of a dispute regarding the nomination of the chairman of the arbitration tribunal, an application shall be submitted to the District Court of Reykjavik for a ruling to resolve the dispute.

The cost of the arbitration process, including the legal costs of the party for whom the tribunal finds, shall be collectible from the opposing party if and to the extent decided by the arbitration tribunal. In other respects the arbitration shall be subject to Act No. 53/1989 on Contractual Arbitration.

The substance of this Contract is confidential. However, this provision shall not prevent the Company from complying with its reporting obligations to the Iceland Stock Exchange pursuant to statutory law or other regulations, or from disclosing the substance of the Contract on the basis of law, rules or court decisions.

So approved at a meeting of the Board of Directors of Icelandair Group hf. on 29 December 2006.

30.3 THE CONSOLIDATED BALANCE SHEET FOR ICELANDAIR GROUP HF. DATED 31 OCTOBER 2006. THE BALANCE SHEET IS INTERNALLY GENERATED AND HAS NOT BEEN AUDITED.

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Balance Sheet as at 31 October 2006

	Icelandair Group	Ice Group Holding	Elimin-ations	Merged Company
Assets:				
Operating assets	22.400			22.400
Intangible assets	16.290		10.400	26.690
Investments in subsidiaries		33.700	(33.700)	0
Investments in associates	1.750			1.750
Prepaid aircraft acquisitions	11.700			11.700
Long-term receivables	1.815			1.815
Total non-current assets	53.955	33.700	(23.300)	64.355
Inventories	1.200			1.200
Trade and other receivables	6.345			6.345
Cash and cash equivalents	4.300	190		4.490
Total current assets	11.845	190	0	12.035
Total assets	65.800	33.890	(23.300)	76.390
Equity:				
Share capital	1.000	1.000	(1.000)	1.000
Share premium	16.350	25.990	(17.117)	25.223
Other reserves	767	120		887
Retained earnings	5.183	(53)	(5.183)	(53)
Total equity	23.300	27.057	(23.300)	27.057
Liabilities:				
Credit institutions	11.200	6.614		17.814
Deferred income tax liability	1.000			1.000
Total non-current liabilities	12.200	6.614		18.814
Credit institutions	3.600			3.600
Trade and other payables	11.100	219		11.319
Current maturities of non-current liabilities	12.200			12.200
Prepaid income	3.400			3.400
Total current liabilities	30.300	219		30.519
Total liabilities	42.500	6.833		49.333
Total equity and liabilities	65.800	33.890	(23.300)	76.390