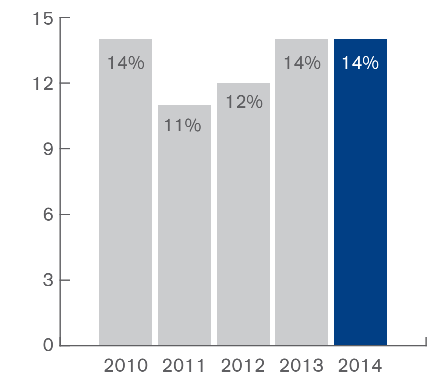
ICELANDAIR GROUP

Annual Report 2014

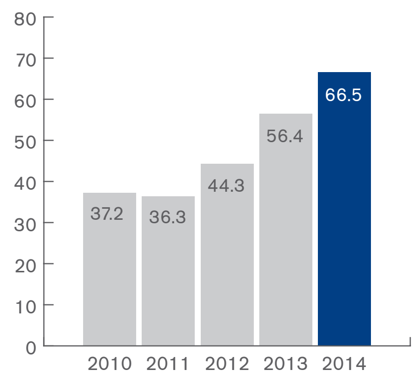
Key Figures

USD thousands	2014	2013	2012	2011	2010
Operating results					
Total income	1,113,297	1,022,957	898,866	790,653	717,904
EBITDAR	193,410	189,870	165,772	144,788	173,361
EBITDA	154,338	143,710	109,646	84,935	102,594
EBIT	79,009	73,011	50,787	38,622	51,011
EBT continuing operations	79,908	71,048	57,448	28,548	53,638
Net profit	66,499	56,418	44,275	36,310	37,162
Balance sheet					
Total assets	849,220	832,875	762,895	729,739	687,104
Total equity	365,055	346,082	295,932	263,385	231,672
Interest bearing debt	61,934	122,017	150,906	196,868	200,685
Net interest bearing debt	-153,707	-77,476	18,112	90,179	94,698
Cash flow					
Net cash from operating activities	215,315	230,874	166,743	117,341	127,838
Net cash used in investing activities	-130,156	-113,223	-76,476	-106,175	-44,959
Net cash used in financing activities	-88,684	-45,232	-51,453	-27,602	-400
Cash and cash equivalents end of year	184,762	191,538	117,060	79,405	95,334
Key ratios					
Earnings per share in US Cent per share	1.34	1.13	0.89	0.73	2.50
Intrinsic value	8.99	8.52	7.29	6.49	5.71
Equity ratio	43%	42%	39%	36%	34%
Current ratio	0.83	0.94	0.94	0.91	1.16
Capex USD thousand	109,293	114,240	95,874	125,008	40,905
Transport revenue as % of total revenues	73%	69%	67%	64%	61%
EBITDAR ratio	17.4%	18.6%	18.4%	18.3%	24.1%
EBITDA ratio	13.9%	14.0%	12.2%	10.7%	14.3%

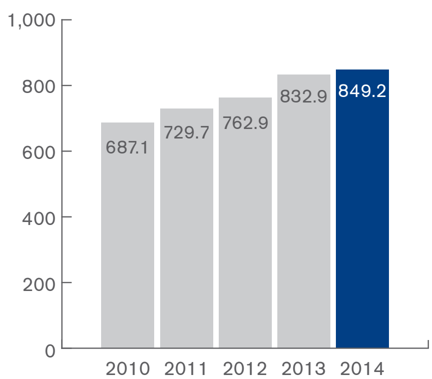
EBITDA % | 2010–2014



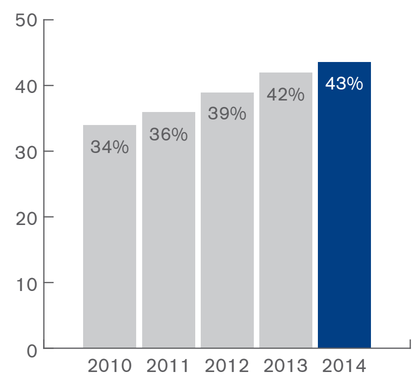
Net profit USD million | 2010–2014



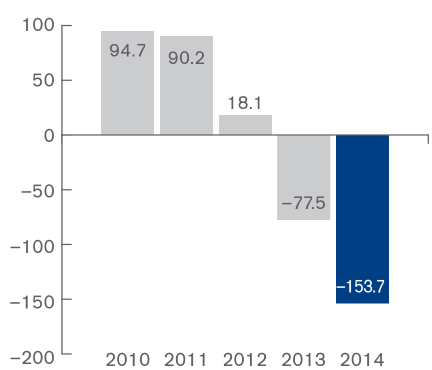
Total assets USD million | 2010–2014



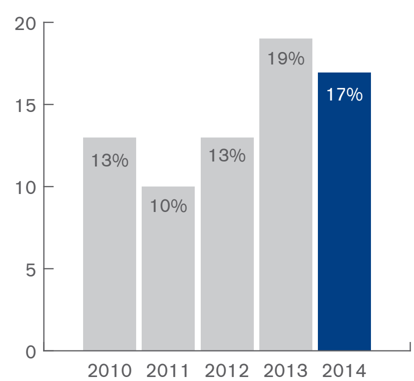
Equity ratio | 2010–2014



Net interest bearing debt USD million | 2010–2014



Cash as % of income | 2010–2014



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About the Annual Report

In Icelandair Group's annual report for 2014 we offer you a glimpse into the breathtaking nature Iceland has to offer, as captured by the photographer Torfi Agnarsson.

Come and be inspired by Iceland.

Design: Íslenska

Photos by Torfi Pictures

Printing: Oddi ehf.

01

STOKKSNES | 64°14'55" N 14°58'39" W

A good prospect can be just as inspiring as a beautiful view.

Our Vision

To unlock Iceland's potential as a year-round destination, to strengthen Iceland's position as a connecting hub and to maintain our focus on flexibility and experience

Letter from the Chairman of the Board of Directors

SIGURÐUR HELGASON,
CHAIRMAN OF THE BOARD
OF DIRECTORS

Fellow shareholders,

The year 2014 was another record year in Icelandair Group's history. For the fifth consecutive year we are returning strong operating results on the back of a 9% growth in revenues. We have continued to enlarge our international fleet, and at the same time we have streamlined our operations, with the result that revenue has grown by 70% and EBITDA by 133% since 2009.

Our foundation remains firm: Icelandair Group is an operating company engaging in diverse flight and tourist services. Through our subsidiaries we hold a strong position across the value chain in international aviation, in domestic air travel, in the Icelandic hotel market and in other areas of tourist services. Our interests are interlinked with the success of Iceland as a tourist destination, and we take pride in our sustained campaign to promote Iceland abroad as a year-round destination.

In 2014 Icelandair Group's EBITDA amounted to USD 154 million, and net profit amounted to USD 67 million, up by 18% between years. The financial position of Icelandair Group has gone from strength to strength, with the Company's equity ratio at 43% and interest-bearing debt reduced by USD 60 million over the year to a year-end figure of USD 62 million. Our strong liquidity and sound balance sheet are instrumental in supporting our profitable growth strategy going forward.

Growing shareholder base and consistent dividend payouts

Our shareholder base has continued to expand, and the number of our shareholders was 2,099 at year-end, including Iceland's largest pension funds. Through pension fund holdings in Icelandair Group the vast majority of Icelanders have reaped the financial benefits of our sound operations for the last five years. As a testament to our success, the number of our shareholders increased by over 15% in 2014, the Company's share price increased by 18%, and its market capitalisation increased from ISK 91 billion to ISK 107 billion over the course of the year. Since the share capital increase in 2010 the market capitalisation of Icelandair Group has increased by a multiple of 8.6 over the course of five years.

In accordance with its dividend policy, the Board of Directors has proposed a dividend payment of USD 19.8 million to shareholders in 2015. Since the Board of Directors approved Icelandair Group's dividend policy in 2011, the Company has returned USD 37 million to its shareholders. Factoring in dividend payments to shareholders, the total shareholder return in 2014 amounted to 19%.

In 2015 Icelandair Group has its sights set on continued profitable organic growth, and the Board of Directors continues to be grateful to shareholders for their unwavering support and commitment to the Group's strategic direction. Creating sustainable shareholder value remains at the centre of our organic expansion strategy.

Continued commitment to connecting Iceland

Dedication to Iceland lies at the heart of our business model. Our dedication has been instrumental in developing tourism as the driving force of the Icelandic economy and its largest export sector. We take pride in actively developing and promoting Iceland as a world-class destination. Iceland is high on the list of the IATA connectivity index, showing that Iceland enjoys remarkably high levels of air connectivity relative to the size of its economy. Air connectivity is a measure of the number of routes, range of destinations served, frequency of services and overall capacity deployed to and from a country. The better connected a country is, the greater its ability to take advantage of the benefits that air transport can unlock. There are still untapped opportunities for us to harness.

Our business efforts are firmly grounded in the Icelandair Group vision statement. Our vision is to unlock Iceland's potential as a year-round destination, to strengthen Iceland's position as a connecting hub and to maintain our focus on flexibility and experience, the qualities that have taken us where we are now. We continue to be a company that champions innovation in all our operations.

In 2014 we continued to strengthen our infrastructure for the future. Continued development of Keflavik Airport is vital to support Icelandair Group's ambitious future goals. Investment in aviation and tourism infrastructure needs to become a higher priority going forward, as tourism, made possible by aviation, has become the most important pillar of the Icelandic economy.

Route Network expansion continues

There is underlying turmoil in the global economy. It remains to be seen whether the European Central Bank's quantitative easing will revamp the Eurozone economy and fend off deflationary pressures. On the other hand, there seems to be growing momentum for continued appreciation of the US dollar in the wake of a seismic downward shift in oil prices. The possibility of a Euro-dollar parity calls for adjustments in the global economy. These trends can both create opportunities and pose threats for Icelandair Group, which has shown time and again its ability to adapt quickly to changing external factors.

At the back of these shifts, Icelandair Group remains steadfast in continuing its profitable growth into 2015. The 2015 schedule of Icelandair shows a 14% growth from last year, and the number of passengers is now projected at 3 million, as compared to 2.6 million in 2014. The Company will be operating 6,400 flights to Europe and 3,400 flights to North America. The total number of flights in our 2015 schedule is expected to be just around 10,000, up by 3,200 flights since 2012. Since 2010 we have expanded our fleet in the Route Network by 12 aircraft, which means that the fleet will comprise 24 aircraft in 2015. We have systematically increased both the depth and breadth of the Route Network, which in 2015 will connect 14 cities in North America with 25 cities in Europe. The increased frequency has enabled us to strengthen our market position on both sides of the Atlantic. We continue to add new destinations to our Route Network, with the addition of Portland, Oregon, and Birmingham, England, in the 2015 schedule. As before, the increase in flight frequency in our established markets continues to represent the lion's share of our annual expansion. Going forward, there remain significant opportunities for continued profitable growth.

For the last six years we have increased our capacity on the North Atlantic by around 19% on average, while the total market has increased its capacity by around 3%. By growing faster than the market as a whole we have continued to fortify our position as a prominent transatlantic hub and gradually increased our market share in this competitive market.

The introduction of a new fleet, with the first deliveries of Boeing 737 MAX aircraft scheduled in 2018, will create further opportunities for the Company. A mixed fleet of Boeing 757s and Boeing 737 MAX aircraft will suit our Route Network perfectly, as the entire fleet will have the reach needed to fly to both Europe and North America from the central hub in Iceland. The new aircraft will be a great addition to the fleet and increase both flexibility and capacity for growth through added frequency and new destinations.

The new fleet will significantly increase the flexibility of the international Route Network, as the 737's are well suited to increase frequencies to smaller destinations in Europe. The Boeing 757 has long since proven its viability in the Route Network, and coupled with the oil price decline it will remain a good choice well into the next decade for Icelandair.

Growing momentum of connectivity

Since 1987 the Group's international Route Network has developed and expanded, both in breadth and depth. The business model of Icelandair Group's international Route Network focuses on three markets – the tourist market TO Iceland, the domestic market FROM Iceland and the fastest growing VIA market on the transatlantic route between Europe and North America through Iceland. In that regard it is essential to underline the increase in connectivity options that result from a growing route network.

In 1990 the Route Network comprised 12 destinations with the option of 39 connections for our customers, representing a connectivity multiple of 3.25 relative to each destination. In the millennium year the international Route Network comprised 17 destinations, but the connectivity options rose to 83, equalling a connectivity multiple of 4.8 times the number of destinations. A decade and a half later, the 2015 schedule now comprises 39 destinations offering our customers 347 connection options – an astounding connectivity multiple of 8.9 times the number of destinations.

Capitalising on new opportunities

Our operations have both grown and strengthened significantly over the course of the last half decade. I firmly believe that we are fast approaching the critical size needed to be positioned to benefit even more from growth initiatives. The underlying story of the connectivity on offer in our international Route Network is telling for the scalability of our unique business model that gains traction as the number of destinations in our Route Network increases. The connectivity of the Network as a whole is unquestionably larger than the sum of its individual parts.

With our strong balance sheet and robust cash flow we are in a position of strength to take on new infrastructure investments and the operation of a dual fleet from 2018 and onwards. A different fleet setup will play to the strengths of our business model – increasing our flexibility and giving us an opportunity to develop new markets with increased frequency in our Route Network. Our unwavering dedication to excellence has stood the test of time and will continue to do so and support our commitment to connecting Iceland with the world.

On behalf of the Board of Directors of Icelandair Group, I would like to extend our gratitude to our shareholders, our employees and all our other stakeholders for their invaluable contribution to Icelandair Group's continuing success. ■

Letter from the President and CEO

BJÖRGÓLFUR JÓHANNSSON
PRESIDENT AND CEO

Fellow shareholders,

Icelandair Group's operating result in 2014 is a testament to the underlying profitability of our business model. For the fifth consecutive year we are reporting double digit growth in key financial metrics. EBITDA came in at USD 154 million, and net profit amounted to USD 67 million on the back of USD 1.1 billion in revenues.

The impact on our stakeholders throughout the value chain remains the lens through which we evaluate the success of our efforts. In all our endeavours we strive to strike the right chord of achieving short-term profitability while maintaining a firm foundation for longer-term sustainable growth. We emphasise the importance of cost control and innovation in the entire travel experience for the satisfaction of our customers.

As I have consistently stated, our long-term focus is on delivering sustainable shareholder value throughout the business cycle. We remain proud of our Company's success, and we believe that we can continue our profitable growth by developing new opportunities for the benefit of all of our stakeholders. We remain strategically well positioned to continue our profitable organic growth, even as the competition we face continues to intensify.

We focus on continuous improvements in our operations and we continue to re-evaluate the way we do business. We innovate. We push the envelope in our marketing efforts. We do things better than we did them before. The growth we have delivered over the past half decade has tried and tested our corporate culture, but I believe we have never before been as well positioned to capture and capitalise on new opportunities. Our success has been based on sound decision making and forward-looking strategic planning in combination with positive external factors. Our exceptional workforce has reacted to the changing contours of the competitive landscape, and in many ways they have created and seized opportunities above and beyond any reasonable expectations.

Strong financial result

The Company's financial result in 2014 was strong and the year as a whole saw profitable organic growth, as laid down in our business strategy. For the second year in a row total income surpassed USD 1 billion and registered at USD 1.1 billion, up by 9% between years. EBITDA amounted to USD 154 million, up from USD 144 million last year, which corresponds to a 7% increase. Icelandair Group's aggregate EBITDA currently stands at USD 662 million since 2009, which is a testament to the strength of the Company's underlying operations.

As before, the strong financial results have strengthened the Company's balance sheet, and equity now stands at USD 365 million, total assets amount to USD 849 million and the equity ratio was 43% at year-end 2014. Net interest-bearing debt was negative by USD 154 million, and the Company had USD 216 million available in cash and marketable securities at the end of the year.

Sound strategic direction

The Company's largest market in international flight services is the market between Europe and North America, which has been the principal driving force of our growth in recent years. The market to Iceland has also shown significant growth, and the demand for domestic tourist services has increased rapidly. Concurrently with this expansion, the individual companies forming Icelandair Group have found opportunities for profitable growth. Although Icelandair Group has grown in size in the last five years, we still see ample opportunities for further profitable growth on the horizon.

Oil prices declined sharply in 2014, triggered by OPEC's announcement that supply to the market would no longer be controlled. In addition, a sustained economic pessimism has also contributed to this trend. The ongoing positive supply shock has driven jet fuel prices down. As fuel is a sizable input in our cost structure, such price movements can have a significant impact on our operations in the longer term.

Consistently delivering on promises

Since Icelandair Group's dividend payment policy was approved at the annual general meeting in 2011 the Company has returned USD 37 million in dividend payments to shareholders. The aggregate pay-out equals US Cents 0.77 per share, and the dividend pay-out has added 24% to shareholder returns over the period. The Board of Directors is proposing a USD 19.8 million dividend payment to shareholders this year, which is in line with the Company's dividend policy.

In my address to shareholders in 2013,

I spoke of decisive steps underway at Icelandair Group to address the seasonal fluctuations facing Icelandic tourism. In 2014 we addressed these fluctuations more decisively than ever before by increasing our capacity outside the summer season by 18% – the steepest increase ever outside the summer season. This further underlines our aspirations for Iceland as an attractive and sustainable year-round tourist destination.

Analysis of Icelandair Group's capacity increases in the transatlantic market reveals that the Company has managed to reduce significantly the seasonal fluctuations between the high season in the summer and the lower season in the winter, spring and fall. We will continue on this path, as it is our route to increased profitability through better utilisation of our fixed assets. In line with this strategy, 2015 will see continued emphasis on Route Network expansion and increased investments in Iceland's tourist infrastructure.

Exciting times ahead

I remain a firm believer in the opportunities that lie in strengthening our connecting hub in Iceland for the benefit of Icelandic tourism as a whole. As I have stated, time and again, our international Route Network is increasingly benefitting from economies of scale as our international operations have more than doubled since 2009. By striking the right chord in balancing increased breadth with the introduction of new destinations and increasing the depth of the network by consistently increasing flight frequency, we will strengthen our operating efficiencies on the transatlantic market through our connecting hub in Keflavik.

A larger network with added frequency is one of the principal catalysts for continued all-year growth in Icelandic tourism. Although our business environment is inherently seasonal we have systematically addressed the seasonality by increasing the supply in our Route Network in the winter, spring and fall – in excess of the high-season increase – to the benefit of Iceland as a year-round tourist destination. Our varied tourist-related companies have continued to develop their product offerings with increased focus on more affluent tourists. We have developed niche marketing efforts, and our tourist infrastructure investments are focused on quality offerings. Our focus is on doing fewer things better.

Since the 1960s we have invited and encouraged our transatlantic passengers to make the most of their travelling time by enjoying a stopover in Iceland. In 2014 we redoubled our efforts to offer our clients to take advantage of the option of stopping in our beautiful home country for up to seven nights at no additional air fare cost. With our transatlantic connections growing at their fastest rate in years, we see a significant opportunity to further promote year-round tourism in Iceland. In addition, the expected growth in tourism to Greenland will pave the way for further establishing Iceland as a hub for tourism in Greenland.

These are exciting times. For the last half a decade we have witnessed the emergence of aviation and tourism as the leading growth segment in the Icelandic economy. The competition is growing, however, and although external factors are expected to remain positive we believe competitive pressures will continue to increase. It remains to be seen what effects the drop in oil prices will have on capacity changes in the overall market and whether the stimulating effects of the monetary easing of the European Central Bank will materialise in the European economies. External factors will always remain essentially random and unexpected. The ability to respond to these external factors is what will separate the wheat from the chaff in the tourism and aviation industry.

Our continued growth is inextricably linked to the overall success of Iceland as a tourist destination and our growth as a connecting hub in the North-Atlantic. Our 3,100 strong workforce remains dedicated to doing better each year. The culture of our Company has never been stronger, and our dedication to excellence is unwavering. Icelandair Group will remain steadfast going forward in its focus on expanding Iceland's role as a connecting hub and on marketing the country as a year-round tourist destination for the benefit of all of our stakeholders.

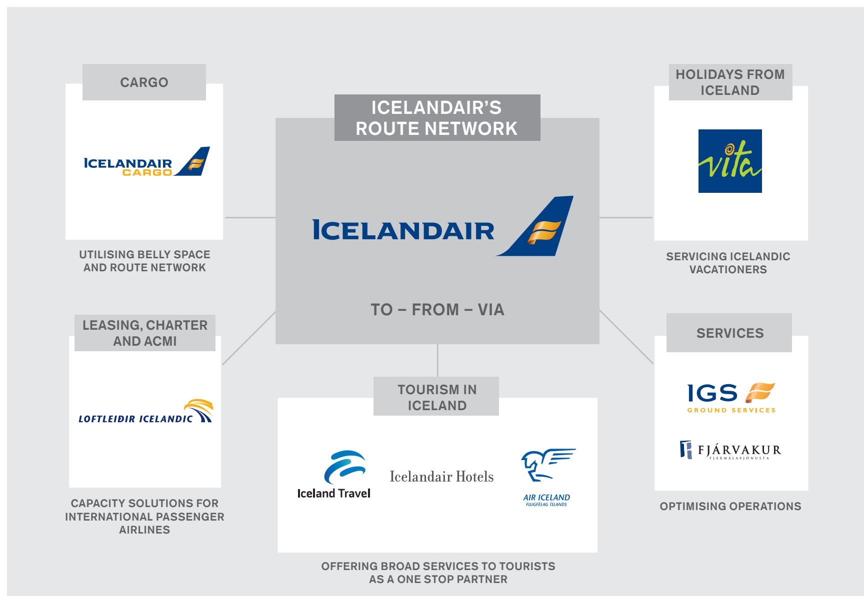
02 RAUFARFELLSVEGUR | 63°31'44" N 19°36'15" W

Farmlands by the foothills of the famous Eyjafjallajökull.

We are Icelandair Group

Icelandair Group operates in the international airline and tourism sectors, with Iceland as the focal point of its international Route Network. We believe that our current portfolio of companies in the aviation and tourist services is both stable and mutually reinforcing, but it remains critical for the Group to retain a high level of flexibility to adapt to unforeseen changes in the market environment.

Icelandair Group's business concept is built on Icelandair's Route Network and on marketing Iceland as a year-round destination. In 2014 the Group employed an average of 3,109 full-time employees, generated total revenues in excess of USD 1.1 billion and carried approximately 2.9 million passengers on its international and regional flights.



Icelandair Group is the parent company of nine subsidiaries covering the two business segments of Route Network and Tourism Services.

The main focus of the Route Network is to operate flights based on the Hub and Spoke concept between Europe and North America via Iceland. The focus of the Tourist Services business segment is on catering to the growing demand for universal services to tourists in Iceland and on offering a wide variety of support services relating to airline operations.

In addition to the passenger flights operated by Icelandair, the Group has extensive interests in most other parts of Icelandic tourism and aviation, including hotel chains, travel agencies, regional airline and cargo, support services and ground handling and technical services, in addition to its leasing and charter operations.

The Route Network is our cornerstone
In 2014 we flew to 39 destinations in our international Route Network, 13 in the USA and Canada and 26 in Europe. Our Route Network is based on a 24-hour rotation with morning and afternoon connections through the hub in Iceland.

At year-end 2014 the fleet consisted of 37 aircraft, with 28 aircraft owned by the Group and 9 aircraft on lease.

Our strategy
Our strategy is regularly and continually tested in order to enable Icelandair Group to fully understand the competitive market in which we operate and to take advantage of any hidden opportunities that may exist and any new opportunities that may arise. To this end we strive to develop tools that will enable us to create more value than our competitors for the benefit of all of our stakeholders.

THE GROUP'S LONG-TERM STRATEGY REMAINS FIRMLY CENTRED ON FIVE KEY POINTS:

- **#1** Focusing on the Route Network and Tourism Services
- **#2** Reducing seasonality in the Group's operations
- **#3** Focusing on organic growth and business development
- **#4** Achieving greater synergies between Group companies
- **#5** Improving efficiency with special emphasis on continuous cost control

Our building blocks of sustainable shareholder value

Icelandair Group's strategy can be graphically illustrated in the shape of tapering building blocks, rising in hierarchical order to show our approach to the Company's strategic development from the ground up. At the base is the day-to-day focus of our employees on current operations and at the top is our vision for Icelandair Group.

Our building blocks of sustainable shareholder value

Vision	What we aspire to become
Operating pillars	The source of our strength
Values	How we conduct our business
Goals	How we evaluate our efforts
Strategic Initiatives	Our day-to-day focus

The top three building blocks represent our long-term aspirations and corporate conduct. They are the core of our competitive advantage and they determine how we structure our operations to leverage our strengths. In essence, they determine our strategic direction and serve as the lens through which we evaluate new projects and strategic initiatives.

The bottom two building blocks represent our short-term focus on profitable operation. They are revised annually and updated to capitalise on emerging short-term and long-term trends. The strategic initiatives are the engine that drives the long-term strategic trajectory of the Group and the goals provide us with important checkpoints along the way to monitor our progress.

Vision statement

Our vision statement encapsulates our aspirations and is a powerful tool to rally all our stakeholders around a set of common goals. It reflects our ambitions and quantifies our goal for the future.

- Destination and schedule growth focused on strengthening the Iceland hub.
- Reducing the seasonality of tourism to improve utilisation of assets.

To unlock Iceland's potential as a year-round destination, to strengthen Iceland's position as a connecting hub and to maintain our focus on flexibility and experience

- Fully leveraging flexibility across subsidiaries to deliver maximum value for the Group.
- The experience of our employees and over 78 years of operating experience set us apart from the competition.

The vision belongs to Icelandair Group as a whole, and all our employees contribute to its realisation. Through our goals and strategic initiatives we translate our aspirations into actions that can be measured and managed throughout the business cycle.

The essence of our vision encompasses the focal points of our business concept of leveraging our strengths; to us, these points are much more than mere words on paper.

- **Year-round tourist destination**
  Icelandair Group has been at the forefront of devising a long-term strategy for Iceland as world-class destination, and through our investments in Icelandic tourism we have played a leading role in a sustained campaign of development and promotion that benefits not only our own operations but the entire Icelandic travel industry.

- **Strengthen Iceland as a connecting hub**
  Steadily expanding Icelandair's Route Network, which has grown by 16 destinations from the year 2009 is the Group's key to enhancing Iceland's position as an international connecting hub.

- **Focus on flexibility and experience**
  Our continued leveraging of the experience of our unique talent pool remains our primary source of strength, as our employees have proven time and again.

Operating pillars of Icelandair Group

Our vision can be depicted as a structure resting on three pillars: the growth of Icelandic tourism, the growth of connecting VIA traffic and a combination of flexibility and experience.

Sustainable value creation for our shareholders and other stakeholders lies at the heart of our organisation. The best way for us to succeed in this effort is to maintain our traditional dedication and commitment to connecting Iceland with the world by drawing on the strength of our operating pillars.

Icelandair Group has supporting subsidiaries that provide capabilities which enable the Group to expand its profitable operations.

VALUES

Our core values are grounded in the philosophy that guides our internal conduct as well as our external relations with our customers, partners, shareholders and other stakeholders.

WE CARE
For our customers, employees, environment and shareholders

WE THINK CLIENTS
Through consistency, reliability, clear product alternatives and friendly service

WE DRIVE RESULTS
Via teamwork, shared information and values, accountability and profitability

What we do, what we say, and how we behave determines how our customers see us. Our behaviour is the practical manifestation of our brand and reflects our values.

Goals and strategic initiatives

What Icelandair Group needs to do in order to thrive in its competitive landscape is dictated by financial objectives which are universal and apply in all business operations, but these objectives do not in themselves suggest business strategies, nor do they provide strategic direction. Through continuous strategic development, Icelandair Group seeks to preserve its strong market position and continue to grow its profitable operations.

We evaluate our effort by comparison with clear-cut short-term and longer-term financial and operational goals that we translate into our EBITDA projection, which is published annually.

Selected ongoing strategic initiatives of Icelandair Group

- Increase the breadth and depth of the Route Network
- Constant development and more quality in our hotel business
- Expand and renew logistical infrastructure at our hub in Keflavik
- Continue ISO 14001 implementation in all subsidiaries
- Focus on corporate governance
- Support and develop marketing initiative for more affluent customers
- LEAN management initiatives to improve operational efficiencies

We believe that one of our principal strengths lies in our employees. Our operations require a wide range of knowledge and specialised skills in aviation, hospitality, international marketing, finance and management. For this reason we are committed to making Icelandair Group an attractive workplace for our employees. Our success is reflected in the fact that on average our employees have been with the Company for almost 10 years.

Every day we strive to meet the needs of our customers in business and tourism. Icelandair Group is proud of its role in the Icelandic community and continues to seek new opportunities to strengthen its business.

That is our job, around the clock, all year round, all over the world. ■

03

HVÍTÁ IN BORGARFJÖRÐUR | 64°42'50'' N 20°50'1'' W

You can find peace and quiet in Iceland without much effort.

Corporate Governance

AUDIT COMMITTEE:

Katrín Olga Jóhannesdóttir, Chairman

Ásthildur Otharsdóttir

Magnús Magnússon

COMPENSATION COMMITTEE:

Sigurdur Helgason, Chairman

Úlfar Steindórsson

EXEMPLARY IN CORPORATE GOVERNANCE

The Framework
The Guidelines on Corporate Governance issued by the Iceland Chamber of Commerce, NASDAQ OMX Iceland and the Confederation of Icelandic Employers, along with the Company's Articles of Association and Rules for Issuers of Securities listed on the NASDAQ OMX Iceland, make up the framework for Icelandair Group's Corporate Governance practices. The Company's Articles of Association are available on the Group's website and the Guidelines and Rules for Issuers can be accessed on the NASDAQ OMX Iceland website.

The Iceland Chamber of Commerce, the Confederation of Icelandic Employers and the Centre for Corporate Governance at the University of Iceland awarded Icelandair Group for their "Exemplary in Corporate Governance" was recognition in 2013. Icelandair Group was the first listed company in Iceland to receive this recognition.

The Company complies in all main respects with the rules cited above. However, the Company does not have a Nomination Committee, as the Board of Directors has not seen the need for such a committee.

Internal Audit and Risk Management
The Group's Audit Committee oversees management's monitoring of compliance with the Group's risk management policies and procedures and reviews the adequacy of the risk management framework with regard to the risks faced by the Group. The Group's Audit Committee is assisted in its oversight role by Internal Audit. Internal Audit undertakes both regular and ad hoc reviews of risk management controls and procedures, the results of which are reported to the Audit Committee. The committee is entrusted with oversight of the Group's consolidated accounts. The committee is also responsible for evaluation of the independence and eligibility of both the Company´s auditor and auditing firm. The committee submits recommendations to the Board of Directors regarding the selection of the Company´s auditor. The Audit Committee meets on average six times a year.

Values, Code of Ethics and Corporate Responsibility
The Company's values are:

WE CARE for our customers, employees, environment and shareholders;

WE THINK CLIENTS through consistency, reliability, clear product alternatives and friendly service;

WE DRIVE RESULTS via teamwork, shared information and values, accountability and profitability.

On 25 May 2009 the Board of Directors approved a Code of Ethics, which was amended on 5 January 2011. The Code of Ethics is accessible to all the Company's employees through the Icelandair Group intranet, MyWork.

Compensation Committee
The purpose of the Compensation Committee is to avoid the Company's management being placed in control of their own remuneration and to ensure that management's remuneration is structured so as to serve the long-term interests of shareholders. The main tasks of the Compensation Committee are policy making with respect to the management's performance-related bonuses, including stock options. The Committee conducts evaluations of management remuneration and monitors management's acquisition of stock in the Company. The Compensation Committee meets on average four times a year.

The Board of Directors

SIGURÐUR HELGASON, CHAIRMAN

Sigurdur Helgason was President and CEO of Flugleidir/Icelandair 1985 - 2005. He was Director Cash Management 1974 - 1980, Senior Vice-President Finance 1980 - 1983, General Manager The Americas 1983 - 1985 at Flugleidir/Icelandair. He was a member of the IATA Board of Governors 2004/2005. He was a Member of the Board of Directors at Finnair 2007 - 2012. He was Chairman of the Board of The Icelandic International Development Agency 2005 - 2008. He has been Chairman of the Icelandair Special Children Travel Fund since 2005. He has served on various boards of Icelandic business enterprises since 1974. He graduated with an MBA degree from the University of North Carolina, Chapel Hill, USA, in 1973 and completed a Cand. Oecon. degree at the University of Iceland in 1971. He joined the Board on 6 August 2009.

ÚLFAR STEINDÓRSSON, DEPUTY CHAIRMAN

Úlfar Steindórsson is the CEO of Toyota in Iceland and Jú ehf. He was CEO of Primex ehf in Siglufjordur from 2002-2004, and CEO of the New Business Venture Fund in 1999-2002. Úlfar is Chairman of the Board of Eignarhaldsfélagið Bifreiðar, Bergey ehf, Bifreiðainnflutningur ehf, Bílaútleigan ehf, Okkar bílaleiga ehf, and TK bílar ehf. He is a Board Member of Toyota á Íslandi ehf, Krókasslóð ehf, TMH Iceland ehf, AB 257 ehf, Blue Lagoon International ehf, Eldvörp ehf, Hótel Bláa lónið ehf, Bláa Lónið Heilsuvörur ehf, UK fjárfestingar ehf, Johan Rönning hf, S.Guðjónsson ehf and Skorri ehf. Úlfar holds a Cand.Oecon. degree from the University of Iceland and an MBA from Virginia Commonwealth University. He joined the Board on 15 September 2010.

ÁSTHILDUR M. OTHARSDÓTTIR, BOARD MEMBER

Ásthildur is an independent Management Consultant with prior business experience as Global Director of Treasury and Corporate Development at Össur hf, Senior Account Manager at Kaupthing Bank hf and Management Consultant at Accenture in Copenhagen. She is Chairman of the Board of Directors of Marel hf. and a member of the Board of Directors of Marorka ehf, and the Research Centre for Business Ethics at the University of Iceland. Ásthildur has an MBA degree from the Rotterdam School of Management, Erasmus University and a Cand. Oecon. degree from the University of Iceland. She joined the Board on 23 March 2012.

KATRÍN OLGA JÓHANNESDÓTTIR, BOARD MEMBER

Katrín Olga Johannesdóttir is the former Chief Strategy Officer of Skipti hf and the current Chairman of Já upplýsingaveitur hf. Before that she was VP for sales and marketing and VP for residential markets at Síminn hf. Prior to that she held a position as the Managing Director of Navision Iceland and was a management consultant at VSO. Katrin Olga currently serves on the Boards of Directors of Ölgerðin hf, Reykjavik University, the Iceland Chamber of Commerce, Advania and Njála ehf, having previously served on the Boards of the Central Bank of Iceland, Sirius IT and SkjáMiðlar. She holds a Cand.Oecon. degree from the University of Iceland and an M.Sc. in Business Economics from Odense University. She joined the Board on 6 August 2009.

MAGNÚS MAGNÚSSON BOARD MEMBER

Magnús has been employed as a Division Manager at LBI hf since early 2009, having previously worked for Búnadarbankinn and the financing company Lýsing following a period of self-employment from 2003 to year-end 2008. Magnús currently serves on the Board of Directors of Lýsi hf and the manufacturing and contracting company Loftorka in Borgarnes, as well as several subsidiaries of LBI hf. Magnús holds a degree in Business Economics from the University of Iceland and a Masters Degree in International Business from Norges Handelshøyskole. Magnús has been a reserve member of Icelandair Group's Board of Directors since 2009 and a full member of the Board since fall 2014.

The Board of Directors, continued:

The Company's Board of Directors exercises the supreme authority in the Company's affairs between shareholders' meetings and is entrusted with the task of ensuring that the organisation and activities of the Company's operation are at all times in correct and proper order.

The Board of Directors is instructed in the Company's Articles of Association to appoint a President and CEO for the Company and to decide on the terms of his or her employment. The Board of Directors and President and CEO are responsible for the management of the Company.

The Company's Board of Directors is required to ensure that there is adequate supervision at all times of the Company's accounts and the use of its assets and shall adopt working procedures in compliance with the Companies Act. Only the Board of Directors has the authority to assign powers of procuration on behalf of the Company. The signatures of the majority of the members of the Board are required to bind the Company. The President and CEO has charge of the day-to-day operation of the Company and is required in his work to observe the policy and instructions set out by the Company's Board of Directors. Day-to-day operation does not include measures which are unusual or extraordinary. Such measures can only be taken by the President and CEO with the specific authorisation of the Board of Directors, unless it is impossible to await the decision of the Board without seriously disadvantaging the operation of the Company. In such instances, the President and CEO is required to consult with the Chairman of the Board, if possible, after which the Board of Directors must immediately be notified of the measures. The President and CEO shall ensure that the accounts and finances of the Company conform to law and accepted practices and that all assets belonging to the Company are securely safeguarded. The President and CEO is required to 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.

The Company's Board of Directors is composed of five members and one alternate member, elected at the annual general meeting for a term of one year. Prospective candidates must inform the Board in writing of their intention to stand for election at least five days before the annual general meeting or extraordinary shareholders' meeting at which elections are scheduled. Only candidates who have informed the Board in advance are eligible.

The Board of Directors elects a Chairman and Deputy Chairman from among its members, and otherwise allocates its duties among its members as needed. The Chairman calls Board meetings. A meeting must also be called at the request of a member of the Board of Directors or the President and CEO. Meetings of the Board are valid if attended by a majority of its members. However, important decisions shall not be taken unless all members of the Board have had an opportunity to discuss the matter, if possible. The outcome of issues is decided by force of vote; in the event of an equality of votes a motion is regarded as rejected. The President and CEO attends meetings of the Board of Directors, even if he or she is not a member of the Board, and has the right to participate in discussions and submit proposals unless otherwise decided by the Board in individual cases. A book of minutes is kept of proceedings at meetings and minutes must be signed by participants in the meeting. A Board member who disagrees with a decision made by the Board of Directors is entitled to have his or her dissenting opinion entered in the book of minutes. The same applies to the President and CEO. The Chairman is responsible for the Board's relations with shareholders and shall inform the Board of views held by shareholders.

On 12 September 2007 the Board of Directors approved Working Procedures for the Board of Directors, which were amended on 15 November 2010. The Rules on Working Procedures are accessible to the Board of Directors and the management through the Board's intranet, Coredata. In accordance with article 14 of the Rules on Working Procedures, the Board of Directors must annually evaluate its own work, number of members, composition and practices, and must also evaluate the performance of the President and CEO and other managers responsible for the day-to-day management of the Company and its development. The annual performance assessment is intended to improve working methods and enhance the efficiency of the Board. The assessment includes evaluation of the strengths and weaknesses of the Board's work and practices and examination of areas where the Board believes there is room for improvement.

The Board of Directors elects the members of two sub-committees: the Compensation Committee and the Audit Committee. The sub-committees are subject to the Rules on Working Procedures. The Board of Directors meets on average twelve times a year, but met 22 times in 2014. All the Members of the Board of Directors, except Ásthildur Otharsdóttir are independent of the Company. All Board members were also independent of the Company's major shareholders in 2014. ■

Executive Committee

BJÖRGÓLFUR JÓHANNSSON
PRESIDENT AND CEO

Before joining Icelandair Group, Björgólfur was CEO of Icelandic Group, an international seafood company, from March 2006. From 1992-1996 he was CFO of UA in Akureyri. He became CEO of Síldarvinnslan, a fisheries and fish processing enterprise in 1999 and served as Director of Innovation and Development at the fisheries company, Samherji from 1996, having worked as an accountant for two auditing firms from 1980. Björgólfur served as Chairman of the Board of the Federation of Icelandic Fishing Vessel Owners from 2003-2008. He was elected Chairman of the Confederation of Icelandic Employers in March 2013. He graduated with a degree in Business Administration from the University of Iceland in 1983 and qualified as a chartered accountant in 1985.

BOGI NILS BOGASON
CFO, ICELANDAIR GROUP

Bogi Nils began his career with Icelandair Group in October 2008. He was CFO of the investment firm Askar Capital from January 2007 until he joined Icelandair Group, and CFO of the international seafood company Icelandic Group, from 2004-2006. Bogi Nils was an auditor and partner at KPMG in Iceland in 1993-2004. He holds a Cand. Oecon. degree in Business from the University of Iceland and qualified as a chartered accountant in 1998.

BIRKIR HÓLM GUÐNASON
CEO, ICELANDAIR

Birkir Hólm Guðnason was appointed CEO of Icelandair in May 2008, after serving with the company from 2000. Earlier posts at Icelandair include Sales Manager in Iceland 2000-2002, Sales & Marketing Manager in North America 2002-2005, General Manager for Central Europe, situated in Frankfurt, 2005-2006, and General Manager for Scandinavia, situated in Copenhagen, from 2006. Birkir studied in Aalborg, Denmark, 1995-2000 and holds a B.Sc. degree in Business Economics and an MBA degree in International Business Economics from Aalborg University. Birkir is the Chairman of the Board of the American Icelandic Chamber of Commerce. He is a member of the Board of the Chamber of Commerce and Íslandsstofa (Promote Iceland).

MAGNEA ÞÓREY HJÁLMARSDÓTTIR
MANAGING DIRECTOR, ICELANDAIR HOTELS

Magnea was appointed Managing Director of Icelandair Hotels in July 2005, having joined Icelandair Hotels in 1994. Magnea has worked in the hotel industry since 1991 and held management positions at hotels in Iceland, Switzerland and Japan. She completed her MBA at the University of Surrey, UK, in 2003.

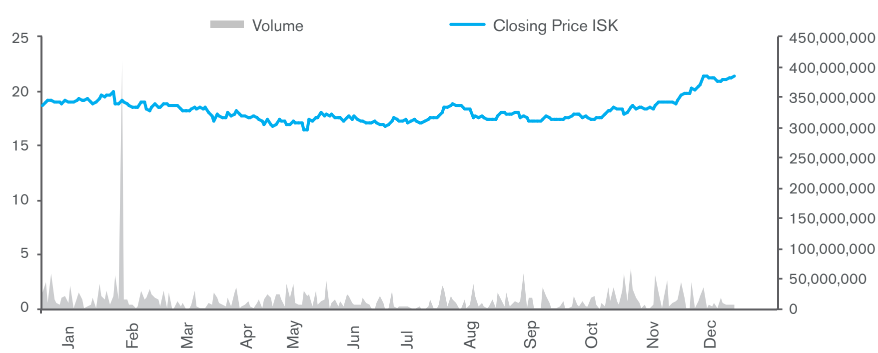
Shareholder information

Icelandair Group's main objective is to create sustainable value for its shareholders. The Group's share price increased by 18% over 2014. In addition, shareholders were paid a dividend amounting to US 0.24 cent per share. At year-end Icelandair Group had the second largest market capitalisation on NASDAQ OMX Iceland.

Share capital
Icelandair Group's share capital as at 31 December 2014 amounted to ISK 5,000 million in nominal value. All shares are of the same class and hold equal rights; each share has a nominal value of ISK 1 and carries one vote. Shareholders are entitled to dividends as declared from time to time. The Company held own shares in the nominal amount of ISK 25 million at year-end 2014 (2013: ISK 25 million). The Group's shares are listed under the code ICEAIR on the NASDAQ OMX Iceland.

Share performance
Over the year Icelandair Group's share price rose from ISK 18.20 to ISK 21.40, an increase of 17.6%. The highest closing price in 2014 was ISK 21.40 per share, the lowest closing price was ISK 16.45 per share and the average closing price over the year was ISK 18.24 per share.

Icelandair Group share price and trading volume | 2014 per month



All amounts in ISK	2014	2013	2012	2011	2010
Market Capitalisation million	107,000	91,000	41,100	25,150	15,750
Share price at year-end	21.40	18.20	8.22	5.03	3.15
Highest closing price	21.40	18.20	8.24	5.18	3.90
Lowest closing price	16.45	8.22	4.83	5.7	2.80
No. of issued shares million	5,000	5,000	5,000	5,000	5,000
No. of outstanding shares million	4,975	4,975	4,975	4,975	4,975
Average no. of outstanding shares million	4,975	4,975	4,975	4,975	1,486

Share liquidity

Icelandair Group has entered into an agreement with Landsbanki hf. and Íslandsbanki hf. regarding market-making for the issued shares of Icelandair Group. The agreement is of unspecified duration and may be terminated with one month's notice. The purpose of the agreement is to improve liquidity and to enhance transparent price formation for the Company's shares on NASDAQ OMX Iceland.

Shares in Icelandair Group were traded 3,929 times in 2014 for a total market value of ISK 71.9 billion (ISK 73.8 billion in 2013). The volume of trading in the shares averaged ISK 290.9 million per day, and the average number of shares traded was 15.8 million. At the end of 2014 Icelandair Group's market capitalisation had reached ISK 107.0 billion.

Key ratios

Icelandair Group reported net shareholder earnings of USD 66.5 million in 2014, corresponding to 1.3 US cents per share. The Company's total equity at year-end was USD 365.0 million. The P/E ratio at the same time was 12.6 and the P/B ratio was 2.4.

	2014	2013	2012	2011	2010
Earnings per share in US Cent	1.3	1.1	0.9	0.7	2.5
Intrinsic value of share capital	9.0	8.5	7.3	6.5	5.7
P/E ratio	12.6	13.9	7.2	5.6	1.0
P/B ratio	2.4	2.1	1.1	0.8	0.6
Number of shareholders	2,099	1,833	1,458	1,269	871

Shareholders

At the end of 2014 the number of shareholders was 2,099, as compared to 1,833 at the beginning of the year. 0.6% of the total shareholder base held 67.6% of the shares in the Company.

Number of shares	Shareholders	%	Shares	%
1 - 100,000	1,405	66.9%	32,678,331	0.7%
100,001 - 1,000,000	527	25.1%	180,220,754	3.6%
1,000,001 - 10,000,000	118	5.6%	332,782,462	6.7%
10,000,001 - 100,000,000	36	1.7%	1,076,066,110	21.5%
100,000,001 +	13	0.6%	3,378,252,343	67.6%
Total	**2,099**	**100.0%**	**5,000,000,000**	**100.0%**

Financial Calendar

Q1 2015 | Week 18, 2015

Q2 2015 | Week 31, 2015

Q3 2015 | Week 44, 2015

Q4 2015 | Week 06, 2016

AGM | Week 11, 2016

20 Largest shareholders 31 December 2014:

Name	No. Shares	Shares in %
Lífeyrissjóður verslunarmanna	729,136,116	14.58
Stefnir - ÍS 15	565,209,103	11.30
Lífeyrissjóður starfsmanna ríkisins	335,670,000	6.71
Stefnir - ÍS 5	325,953,768	6.52
Gildi - lífeyrissjóður	265,041,885	5.30
Stapi lífeyrissjóður	179,977,000	3.60
Stafir lífeyrissjóður	179,614,574	3.59
Íslandssjóðir hf.	163,489,206	3.27
Sameinaði lífeyrissjóðurinn	147,359,671	2.95
Lífeyrissjóður starfsmanna ríkisins	141,031,500	2.82
Íslandsbanki hf.	120,200,281	2.40
Landsbréf - Úrvalsbréf	117,635,501	2.35
A.C.S safnreikningur I	107,933,738	2.16
Söfnunarsjóður lífeyrisréttinda	97,809,131	1.96
Lífeyrissjóður starfsmanna sveitarfélaga	82,668,280	1.65
Straumur fjárfestingabanki hf.	74,894,507	1.50
Virðing safnreikningur	60,914,664	1.22
Festa - lífeyrissjóður	49,657,499	0.99
Landsbréf Öndvegisbréf	42,078,646	0.84
Lífeyrissjóður Vestfirðinga	37,398,556	0.75
Other	1,176,326,374	23.53
Total	**5,000,000,000**	**100.00**

Dividend and dividend policy

Icelandair Group's goal is to pay 20-40% of each year's net profit in dividends. Final annual dividend payments will be based on the financial position of the Company, operating capital requirements and market conditions. This year Icelandair Group's Board of Directors proposes that dividends for the year 2014 totalling ISK 2.5 billion, or USD 19.8 million, should be paid out to shareholders, an amount representing 30% of the net profit for the year. Based on Icelandair Group's share price as at 31 December 2014, ISK 21.4, the dividends correspond to 2.3% of market capitalisation.

Investor relations

Icelandair Group's objective is to ensure that timely and correct information about the Company is made available to all stakeholders simultaneously, regularly and consistently. All financial disclosures and Company announcements are published through GlobeNewswire, a NASDAQ OMX company. Icelandair Group strives continuously to improve the quality, transparency and consistency of its information disclosures.

The Investors' website at www.icelandairgroup.com/Investors/ provides extensive background information on Icelandair Group for both analysts and investors. The site contains the IR-policy of the Company, archived regulatory announcements, financial reports and presentations, shareholder information, share price information, dividend policy and the financial calendar.

Every day we strive to meet the needs of our customers in business and tourism. Icelandair Group is proud of its role in the Icelandic community and continues to seek new opportunities to strengthen its business.

04

LANDMANNALAUGAR | 63°59'32" N 19°3'29" W

A place of contrasting colours and ample supplies of geothermal water.

Performance in 2014

Icelandair Group's 2014 results were good. Net profit amounted to USD 66.5 million, up by USD 10.0 million between years. EBITDA was USD 154.3 million, as compared to USD 143.7 million in 2013. Total income increased by 9% and totalled USD 1.1 billion.

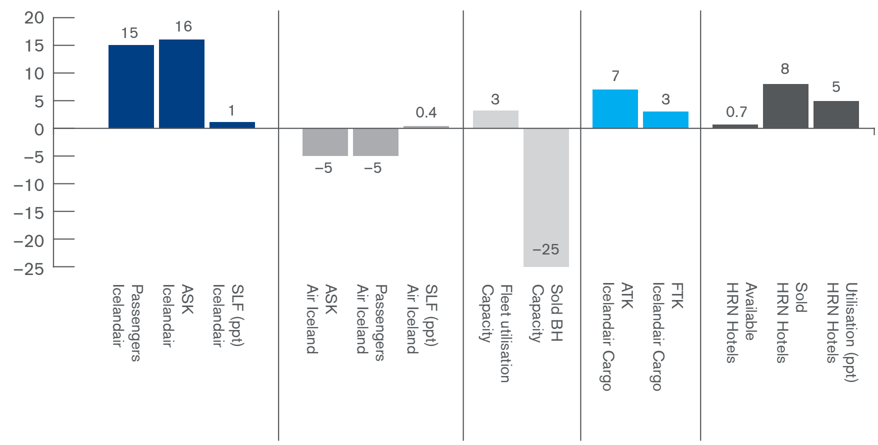
Transport figures

Passengers on international flights were 2.6 million in 2014, up by 15% from the preceding year. The Company has never before transported so many passengers in a single year. The passenger load factor over the year was 80.4%, up by 1.1 percentage points between years. The passenger load factor has only once been higher, in 2012, when the factor was 80.6%. The increase in passenger numbers was greatest in the market between Europe and North America via Iceland, at 23%. This is also the Company's largest market, accounting for 48% of the total number of passengers in 2014.

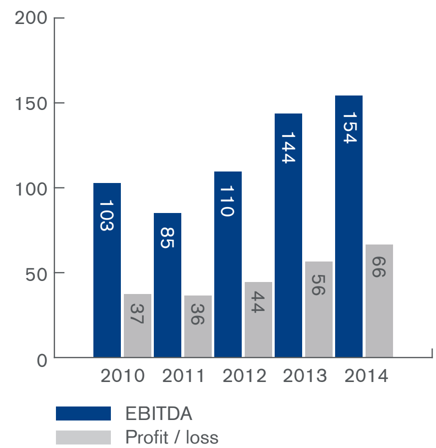
Passengers on domestic flights and flights to Greenland were 293 thousand, as compared to 307 thousand in 2013, which corresponds to a reduction of 5%. The capacity was downscaled between years to respond to the falling demand, bringing the passenger load factor for the year to 71.5%, up by 0.4% from the preceding year. Fleet utilisation in charter projects improved by 3.2 percentage points in 2014, to 94.2%. The number of sold block hours on charter flights fell by a quarter between 2013 and 2014; mainly because the Company discontinued its ACMI cargo operations around mid-year and now concentrates exclusively on cargo operations on scheduled flights. The number of sold hotel nights increased over 2014, by 8%, and amounted to 75.6%, as compared to 70.7% in 2013.

	2014	2013	Change
INTERNATIONAL FLIGHTS			
Number of passengers (´000)	2,605.5	2,257.3	15%
Load factor (%)	80.4	79.3	1.1 ppt
Available seat kilometres (ASK´000,000)	9,673.3	8,320.3	16%
REGIONAL- AND GREENLAND FLIGHTS			
Number of passengers (´000)	292.7	307.3	-5%
Load factor (%)	71.5	71.1	0.4 ppt
Available seat kilometres (ASK´000,000)	147.6	154.5	-5%
CHARTER FLIGHTS			
Fleet Utilisation (%)	94.2	91.0	3.2 ppt
Sold Block Hours	21,044	28,089	-25%
CARGO			
Available Tonne Kilometres (ATK´000)	216,617	201,796	7%
Freight Tonne Kilometres (FTK´000)	97,660	94,787	3%
HOTELS			
Available Hotel Room Nights	316,773	314,603	1%
Sold Hotel Room Nights	239,522	222,320	8%
Utilisation of Hotel Rooms (%)	75.6	70.7	4.9 ppt

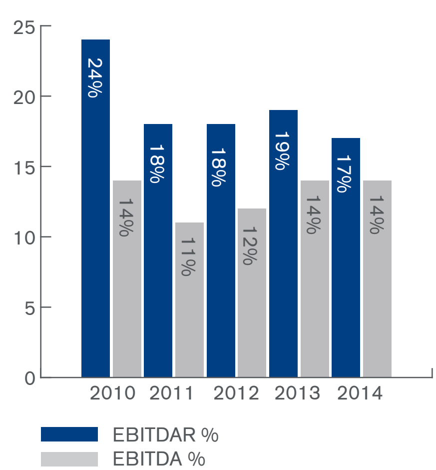
Traffic figures | YOY change in %



EBITDA and net profit
USD millions | 2010–2014



EBITDAR % and EBITDA % | 2010–2014



Earnings

Strong performance in 2014

The year was characterised, like recent years, by profitable organic growth. Net profit amounted to USD 66.5 million, up by 18% from last year. EBITDA amounted to USD 154.3 million, up by 7% between years. The strong performance was the result of a number of interacting positive factors, including falling fuel prices, increased demand in the North Atlantic market – which was met by increased supply – and good results from charter operations. The depreciation of the euro against the US dollar had a negative impact on the Group's operations, and in addition the maintenance cost of cargo aircraft was significantly higher than anticipated.

USD thousand	2014	2013	Change
EBITDAR	193,410	189,870	3,540
EBITDA	154,338	143,710	10,628
EBIT	79,009	73,011	5,998
EBT	79,908	71,048	8,860
Net profit	66,499	56,418	10,081
EBITDAR %	17.4%	18.6%	-1.2 ppt
EBITDA %	13.9%	14.0%	-0.1 ppt

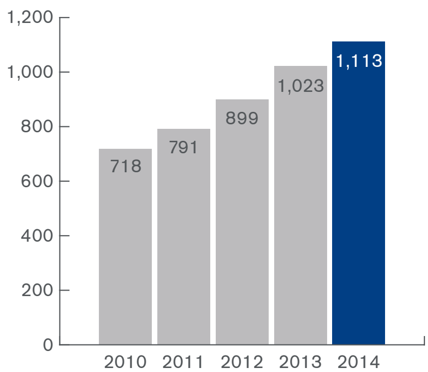
Income

Operating income amounted to USD 1,113.3 million in 2014, increasing by 9% in 2014.

USD thousand	2014	2013	Change	% Change	% of rev. '14
Transport revenue:	811,002	702,882	108,120	15%	73%
Passengers	766,624	659,992	106,632	16%	69%
Cargo and mail	44,378	42,890	1,488	3%	4%
Aircraft and aircrew lease	74,754	117,969	-43,215	-37%	7%
Other operating revenue	227,541	202,106	25,435	13%	20%
Total	**1,113,297**	**1,022,957**	**90,340**	**9%**	**100%**

Performance in 2014, continued:

Total income in USD million | 2010–2014



Passenger revenue up by 16%

Transport revenue totalled USD 811.0 million, up by 15% from 2013. Transport revenue counts for 73% of Icelandair Group's total income. Of this figure, passenger revenues amounted to USD 766.6 million, increasing by 16%. Passenger revenue increased on all of our three markets: the home market from Iceland, the tourist market to Iceland and the market between Europe and North-America.

Charter cargo operations discontinued in 2014

Aircraft and aircrew lease revenue decreased in 2014 by USD 43.2 million, to USD 74.8 million, or by 37%. The main reason is that the Company discontinued its charter cargo operations entirely at mid-year 2014.

Revenue from tourism continues to increase

Other revenue totalled USD 227.5 million in 2014, up by USD 25.4 million from the preceding year, mostly as a result of increased revenue from tourism services and an expanded scope of operation, including increased sales of merchandise in aircraft, in hotels and at airports.

Expenses

Operating expenses amounted to USD 959.0 million in 2014, as compared to USD 879.2 million in 2013, an increase of 9% between years.

USD thousand	2014	2013	Change	% Change	% of exp. ´14
Salaries and other personnel expenses	273,161	239,432	33,729	14%	28%
Aircraft fuel	271,871	242,630	29,241	12%	28%
Aircraft lease	26,653	34,570	-7,917	-23%	3%
Aircraft maintenance expenses	75,884	81,475	-5,591	-7%	8%
Aircraft handling, landing and communication	82,888	74,316	8,572	12%	9%
Other operating expenses	228,502	206,824	21,678	10%	24%
Total	**958,959**	**879,247**	**79,712**	**9%**	**100%**

Salaries and personnel expenses up by 14%

Salaries and other personnel expenses amounted to USD 273.2 million, increasing by USD 33.7 million from 2013. The reason is primarily the Company's increased scope of operation and the contractual salary increases between years. The average number of full-time employees was 3,277 in 2014, as compared to 2,850 in 2013.

Drop in fuel price in second half of 2014

Fuel cost totalled USD 271.9 million in 2014, up by USD 29.2 million compared to 2013. Fuel cost as a percentage of total expenses was 28%. The average world market fuel price in 2014 was 909 USD/Ton, as compared to 990 USD/Ton in 2013. At year-end 2014 the fuel price had dropped to 575 USD/Ton.

Other operating expenses totalled 228.5 million

Other operating expenses increased by USD 21.7 million between years, or 10%. The main explanation is the Company's extended scope of business. Within other operating expenses, advertising, booking fees and commission cost totalled USD 69.1 million, as compared to USD 58.3 million in the preceding year, and tourism expenses increased in line with increased revenue from tourism. The total tourism expenses amounted to USD 50.5 million, increasing by USD 6.2 million from 2013. Other operating expenses decreased by USD 6.7 million between years, mainly due to reversals of bad-debt provisions in the charter operation of Icelandair Group.

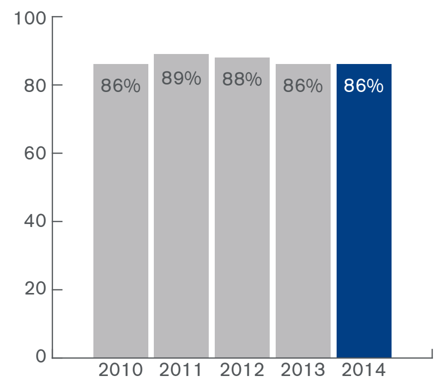
Depreciation and amortisation amounted to USD 75.3 million

Total depreciation of operating assets amounted to USD 71.6 million in 2014, as compared to USD 68.0 million in 2013. Amortisation of intangible assets totalled USD 3.7 million, increasing by USD 1.0 million from 2013. No impairments were made in 2014.

Interest expenses down in 2014

Finance income totalled USD 7.2 million in 2014, as compared to USD 6.8 million in 2013. Of that figure net currency exchange gain amounted to USD 4.8 million in 2014, as compared to USD 4.1 million in 2013. Interest income totalled USD 2.4 million, down from USD 2.7 million in the preceding year. Interest cost decreased by USD 2.6 million, or 30%, from 2013 and amounted to USD 6.1 million.

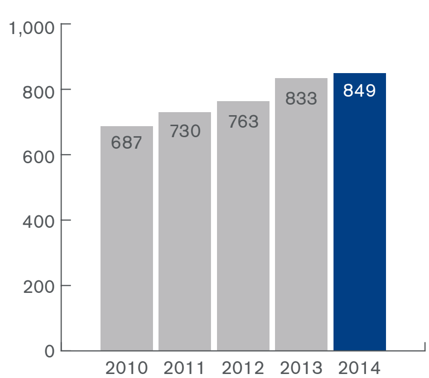
Total expenses before depreciation as % of total income | 2010–2014



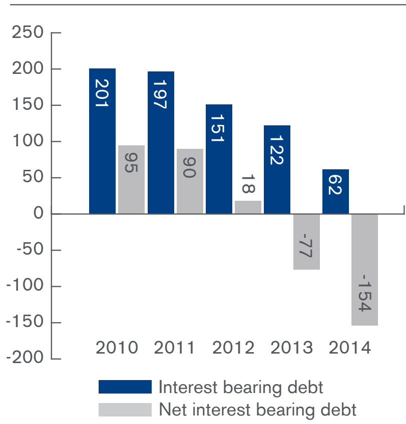
Financial Position

Icelandair Group's balance sheet is strong, showing a 43% equity ratio at year-end 2014. Total assets increased by USD 16.3 million in 2014, to USD 849.2 million, and interest-bearing liabilities at year-end amounted to USD 61.9 million, down by USD 60.1 million from the beginning of 2014. Cash and cash equivalents and short term investments amounted to USD 215.6 million. Total capital expenditures during the year were USD 109.3 million.

Total assets USD million | 2010–2014



Interest bearing and net interest bearing debt USD million | 2010–2014



ASSETS

Assets amounted to USD 849.2 million at year-end 2014

The Group's total assets increased by USD 16.3, million to USD 849.2 million, as compared to year-end 2013. Non-current assets increased by USD 17.2 million, to USD 514.2 million, and current assets decreased by USD 0.9 million, to USD 335.0 million.

Within non-current assets, operating assets increased by USD 20.1 million in the course of the year. The increase is largely a result of the acquisition of two Boeing 757 200 aircraft, aircraft spare parts and capitalised engine overhauls. Intangible assets and goodwill totalled USD 176.0 million, mainly comprising goodwill in the amount of USD 137.1 million. Trademarks and airport slots amounted to USD 33.4 million and other intangibles were USD 5.5 million. Other non-current assets amounted to USD 18.9 million at year-end, slightly above the figure for the preceding year. Of this figure, non-current receivables and deposits amounted to USD 16.4 million.

Within current assets, trade and other receivables decreased by USD 17.8 million from the beginning of the year and totalled USD 96.5 million at year-end 2014. Cash and short term investments increased by USD 16.1 million in the course of 2014, amounting to USD 215.6 million at year-end 2014.

LIABILITIES

Further reduction in interest-bearing liabilities

Non-current liabilities amounted to USD 82.6 million at year-end 2014. Of that figure, loans and borrowings amounted to USD 49.7 million, down from USD 78.5 million at year-end 2013. Current liabilities totalled USD 401.5 million at year-end 2014. Within current liabilities, trade and other payables amounted to USD 214,3 million, as compared to USD 159.5 million at the beginning of the year. Deferred income increased by USD 21.4 million, to USD 174.9 million. Current loans and borrowings decreased between years and amounted to USD 12.3 million at year-end, as compared to USD 43.5 million at the beginning of the year.

Interest-bearing debt totalled USD 61.9 million at year-end 2014. Repayment of long-term liabilities amounted to USD 70.5 million. Net interest-bearing debt was negative at year-end 2014 in the amount of USD 153.7 million, which represents a reduction by USD 76.2 million from year-end 2013.

Net interest-bearing debt:

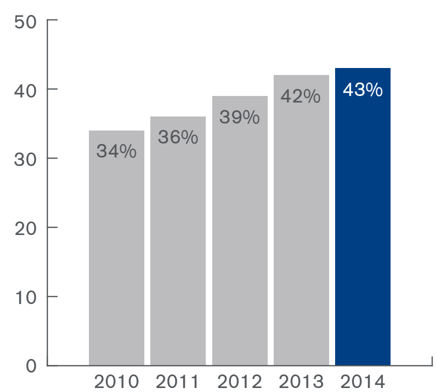
USD	31.12.2014	31.12.2013	Change
Loans and borrowings non-current	49,671	78,489	-28,818
Loans and borrowings current	12,263	43,528	-31,265
Short term investments	-30,879	-7,955	22,924
Cash and cash equivalents	-184,762	-191,538	-6,776
Net interest-bearing debt	**-153,707**	**-77,476**	**-76,231**

Equity

Total equity amounted to USD 365.1 million at 31 December 2014, as compared to USD 346.1 million at the beginning of the year. The largest part of the increase is due to the positive comprehensive income of USD 38.0 million. Dividend payments in 2014 amounted to USD 19.0 million, which is equivalent to 0.38 US Cent per share. The equity ratio was 43%, as compared to 42% in 2013. Share capital at year-end amounted to ISK 5,000 million in nominal value. The Company held own shares in the nominal amount of ISK 25 million at year-end 2014, unchanged from 2013.

USD thousand	2014	2013	2012	2011	2010
Comprehensive income	37,967	69,910	38,854	32,093	17,488
Net profit	66,499	56,418	44,275	36,310	37,162
Equity	365,055	346,082	295,932	263,385	231,672
Equity ratio	43%	42%	39%	36%	34%

Equity ratio | 2010–2014



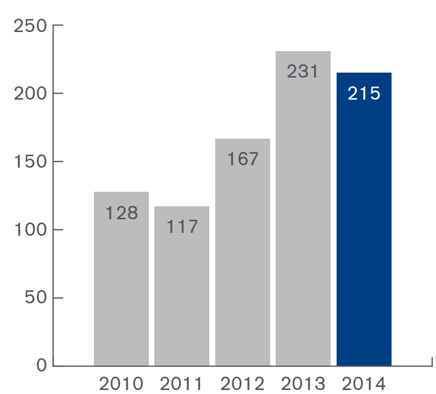
CASH FLOW AND INVESTMENTS

USD thousand	2014	2013	Change
Working capital from operations	162,807	162,385	422
Net cash from operating activities	215,315	230,874	-15,559
Net cash used in investing activities	-130,156	-113,223	-16,933
Net cash used in financing activities	-88,684	-45,232	-43,452
Change in cash and cash equivalents	-3,525	72,419	-75,944
Cash and cash equivalents, end of year	**184,762**	**191,538**	**-6,776**

Cash flow from operations 215.3 million USD

Icelandair Group's cash flow from operating activities came to USD 215.3 million for the reporting year, down from 2013 by USD 15.6 million. Net cash used in financing activities amounted to USD 88.7 million. Of that figure, repayments of long-term borrowings amounted to USD 70.5 million and dividend payments to USD 19.0 million. Cash and cash equivalents at year-end amounted to USD 184.8 million, as compared to USD 191.5 million in 2013.

Cash flow from operating activities
USD million | 2010–2014

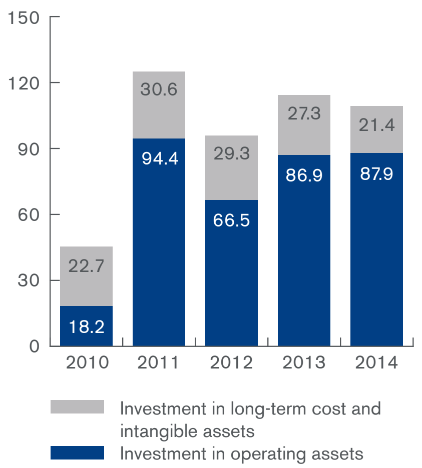


Total investments in 2014 USD 109.3 million

Investments in operating assets amounted to USD 87.9 million. Of this figure, investment in aircraft and aircraft components totalled USD 40.5 million, while investments in engine overhauls on own aircraft totalled USD 29.6 million over the period. Investments in long-term expenses amounted to USD 19.2 billion, largely stemming from overhauls of leased engines. Investment in intangible assets amounted to USD 2.2 million.

Financial Position, continued:

Total investment
USD million | 2010–2014



Fleet

At year-end 2014 Icelandair Group's fleet comprised of 37 aircraft. Of these aircraft, 28 were owned by the Company and 9 were leased. The table below provides an overview of the Company's fleet of aircraft.

In February 2013 the Company signed a contract with Boeing confirming an order of sixteen 737 MAX8 and 737 MAX9 aircraft, with an option to buy an additional eight aircraft. The commitment resulting from the confirmed orders, according to Boeing's list prices, amounts to USD 1.8 billion. The actual purchase price has not been disclosed.

Delivery of the first aircraft is scheduled for early 2018. The order was for nine 737 MAX8 aircraft, with a seating capacity of 153 passengers, and seven 737 MAX9 aircraft, with a seating capacity of 172 passengers. For comparison, Icelandair's Boeing 757-200 aircraft used in the Company's international Route Network has seats for 183 passengers.

The Boeing 737 MAX aircraft are a new and improved version of the current Boeing 737. They will be fitted with new and more efficient engines, which will reduce fuel consumption by 20% per seat in comparison with the Boeing 757-200 aircraft currently used on the Company's international routes.

Boeing 757 aircraft will continue in use, as they have proven extremely well suited for the Route Network extending to Europe and North America. The new aircraft will enlarge the fleet and improve both flexibility and the potential for further growth. Their range will permit them to fly to destinations in North America and Europe, opening new possibilities for increased flight frequency and an increased number of destinations, particularly in the wintertime, which will reduce the seasonal fluctuations in the Company's operations.

Aircraft type	Icelandair	Icelandair Cargo	Loftleidir Icelandic	Flugfélag Íslands Air Iceland	Total
Boeing 757-200	20	2	2		**24**
Boeing 757-300	1				**1**
Boeing 767-300			2		**2**
Boeing 737-700			1		**1**
Boeing 737-800			2		**2**
Fokker 50				5	**5**
Dash 8-200				2	**2**
Total	**21**	**2**	**7**	**7**	**37**

Outlook

Continued organic growth of the Route Network

The prospects for Icelandair Group's operations in 2015 are favourable. Management projections provide for continued profitable growth over the year. The flight schedule for the international Route Network for 2015 plans for a 14% increase in scope between years. Two new destinations will be added in the Network: Portland on the U.S. West Coast and Birmingham in the United Kingdom, together with an increased frequency of flights to current destinations. The number of international passengers is projected at about 3 million in the year, with 24 Boeing 757 aircraft serving the Route Network. Bookings in the first months of the year are off to a good start and in line with the forecast of increased growth.

Favourable prospects for the cargo operations and aircraft leasing

In 2015 the Company's cargo operations will focus on carrying freight on scheduled air services to and from Iceland, as the Company withdrew entirely from cargo ACMI operations in mid-2014. Two cargo aircraft will be used in the operations, together with cargo space in the holds of passenger aircraft on scheduled international routes.

The overall outlook in the aircraft leasing market continues to improve. The emphasis of Icelandair Group's aircraft leasing operation will continue to be on the AM product with sustained effort on the VIP, ACMI & Full Charter markets.

Outlook in the regional airline operations improving

Icelandair Group's regional operations have benefited from the growth in tourist arrivals in Iceland over the last five years. Product development has increasingly been focused on foreign tourists, with marketing efforts concentrated on the offer of a wide variety of day tours and multi-day tours combining domestic and regional flights.

Significant growth in hotel and tourist services

Icelandair Hotels has announced its plans to add around 200 rooms in new hotels in Reykjavik city centre, in addition to the 47-room current expansion of Icelandair Hotel Reykjavik Marina in Reykjavik harbour. The addition of new rooms to the portfolio of Icelandair Hotels will set its mark on the positive development of midtown Reykjavik and deepen Icelandair Group's footprint in the city centre. The Group's operations in tourism-related services is showing success and growing in scope as the number of tourists to Iceland increases and the Route Network grows.

EBITDA forecast for 2015 at USD 160–165 million

The EBITDA forecast for 2015 assumes an increase from 2014 to the range of approximately 160-165 million USD. This forecast assumes an 1.15 average exchange rate of the EUR against the USD in 2014 and an average fuel price of USD 602/ton.

The forecast assumes that the EBITDA ratio will increase between years, to 15.0%-15.5%, as compared to 13.9% in 2014. The reduced fuel price is the single cost item that is chiefly responsible for the increased EBITDA between years. On the other hand, the strengthening of the USD against the European currencies will have a negative impact on the Company's income and earnings.

Risk Management

Icelandair Group's objective in its risk management is to manage and control risk exposures and keep them within acceptable parameters, subject to optimised returns, by using derivatives and other available means. All risk management is carried out within guidelines set by the Board of Directors.

Various financial and enterprise-related risks can impact the Group's operations. The Board of Directors is responsible for defining policy measures to reduce exposure to financial and enterprise risk. These measures outline the parameters and framework which need to be considered when managing risk, especially risk arising from price volatility and liquidity fluctuations. An internal Risk Management Committee, chaired by the CEO, endeavours to reduce risk exposure to the maximum feasible extent within the Board's policy limits. The main policy objectives determine the methods to be used to reduce costs and disadvantages arising from any instability and uncertainty in the Company's operating environment. The policy is reviewed on regular basis and modified when improvements are needed. In 2014 an amended version of the policy was approved by the Board following revision by the Risk Committee. The amendments contribute importantly to improvements in the administration and governance sections of the policy and permit the hedge tenor to be extended from 9 months to 12 months on certain conditions.

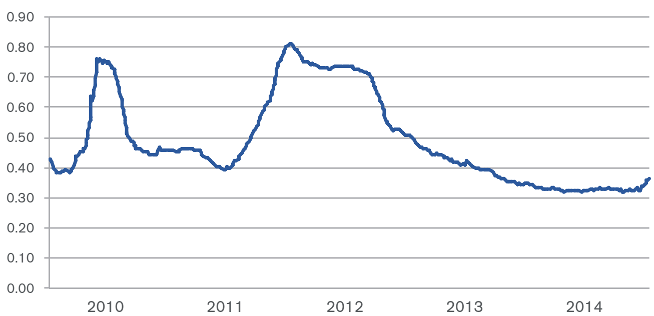
Foreign currency risk

The Group seeks to reduce its foreign exchange exposure arising from its business dealings in diverse currencies through a policy of matching receipts and payments in each individual currency to the extent possible. Any mismatch is dealt with using currency trades within the Group before turning to outside parties. Historically, the biggest currency mismatch has been a USD deficit, where the annual US dollar cash inflow falls short of the dollar outflow by approximately USD 100 million, mainly due to fuel costs, lease payments and funding-related payments, which are to a large extent denominated in US dollars. In relative terms this mismatch has been shrinking as the aggregate nominal amount has remained stable during a period of a steady organic growth since 2009. The gap is expected to shrink further in 2015 due to lower fuel prices and larger USD inflows as a result of increased US sales via marketing and the USD appreciation. In recent years the ISK deficit has emerged and expanded from being trivial to an ISK 15 billion deficit since 2009. This trend stems from the revenue growth in foreign markets whilst the consequential added operations are domestic and need to be covered by ISK. This shortage is financed by a surplus of European currencies, most importantly the EUR and Scandinavian currencies. The Group follows a policy of hedging 40-80% of the net currency exposure 9-12 months forward. In addition to the impact on cash flow, risk exposure of this nature affects the Balance Sheet. The risk committee monitors on a monthly basis the net Balance Sheet currency mismatch and mitigates the exposure through short-term management of assets, loans and liabilities to the extent feasible and within the scope of the cash flow objectives. The revenue currencies inflate the Balance Sheet in the first two quarters of each year due to seasonality and resulting net cash inflows from boosted forward sales matched by accumulated liabilities for owed services. The ISK cash flow mismatch is dealt with by maintaining assets in the same currency.

Fuel price risk

The Group's risk policy requires a hedge ratio between 40 and 60%, 9-12 months forward. Account is taken of the ratio of forward ticket sales as a minimum cover if it exceeds the 40% lower band. The policy entails a mixture of swaps and options, which are allocated in accordance with the degree of risk exposure. The policy and hedge strategy take account of several supporting factors which are eligible to counter the fuel risk

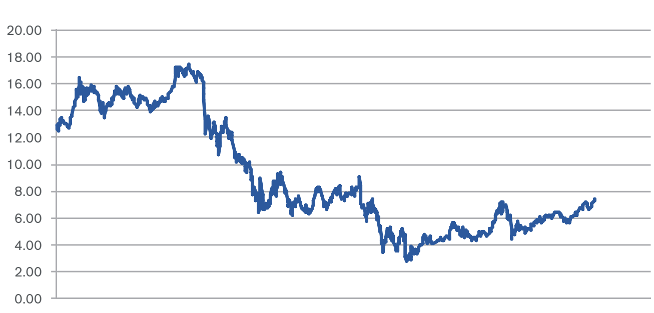
Six month USD libor | 2010–2014



Jet fuel price USD per tonne | 2010–2014

EUR/USD exchange rate | 2010-2014

Carbon price EUR per tonne | 2010–2014



exposure. These factors are acknowledged as hedge proxies and evaluated to some extent as substitutions for hedge contracts. First, contractual risk transfer is used where possible and the benefits of a correlation between jet fuel and the USD are monitored and calculated on a regular basis. Second, ticket pricing is a very important and effective tool in the medium term to offset fluctuations in fuel prices. Third, production management is a longer-term option, which can become relevant when coping with fuel price trends over longer periods. Hedge strategies are subject to IFRS hedge accounting standards but the embedded instrument quality requirements align to some extent with policy guidelines of reporting clarity and the transparency of scenario analysis. Thus, basis risk is avoided and hedge effectiveness sustained by choice of instruments.

Interest rate risk

A considerable share of the Group's outstanding loans is directly related to aircraft financing and denominated in US dollars. The Group follows a policy of hedging 40-80% of the interest rate exposure of long-term financing with up to a 5-year horizon. Currently, foreign loans are hedged against interest rate fluctuations with fixed-rate loan contracts or swap contracts, where the floating rate is exchanged for fixed interest rates. When evaluating the interest risk exposure and the optimal level of contractual protection account is taken of the Group's level of cash and marketable securities and various other offsetting economic factors. As a result of repayments and prepayments of loans in 2014 the capital structure has changed considerably and interest payments are currently of little significance. However, due to future investments steps have been taken to prepare for future funding and to contemplate rate protection measures to meet the

Risk Management, continued:

consequential growth in interest rate exposure. Various strategies and instruments to cover future interest risks have been evaluated but these still fall outside the policy framework in terms of tenor. However, in light of the recent attractive low-rate environment the issue has deserved close attention and policy exemptions provide some scope for action when or if desirable.

Carbon price risk

From the beginning of 2012, all airlines offering European destinations were required to comply with the EU Emissions Trading Scheme (ETS), which commits them to raise their carbon permits in proportion to their emissions of carbon. Icelandair Group is already hedged against roughly 45% of its 2015 exposure through the EU allocations of emissions quotas. In November 2012 the EU decided to offer airlines flying to and from European destinations an exemption from the Scheme with respect to international flights. Icelandair accepted this offer and its commitment was therefore reduced to covering internal European flights. Again, in April 2014, the EU extended this exemption to 2016 and has therefore relieved airlines temporarily from the uncertainty of the carbon exposures within this time frame. Emission permits are mainly purchased with spot and forward contracts, and carbon exposure is subject to the same scrutiny and risk management as jet fuel. However, while the consequences of the ETS compliance is economically trivial in comparison with the magnitude of fuel cost volatility, the emission allowances will not be imbedded into the fuel hedge strategies yet, but instead procured on a rolling 3-6 month basis in relation to fuel consumption.

Liquidity risk

The Group's policy on liquidity risk extends to three asset classes, determined by duration. Those classes are matched against the Group's liquidity targets as defined by the Board of Directors on an annual basis. Classes one and two include the estimated minimum of accessible funds for immediate operational liquidity and reserve purposes. Class three includes assets of longer duration for strategic liquidity, such as medium-term investments. The target amounts in each class of assets are set once a year, subject to a minimum cash level reflecting the estimated 3-month operating costs. This requirement is offset to a certain limit by the access to a short term loan facility.

Credit risk

Credit risk is linked to the amount of outstanding trade receivables, allocation of liquid funds and financial assets and agreements with financial institutions relating to financial operations, e.g. credit support annexes concerning hedging. The relative spread of trade receivables across counterparties is also crucial for credit risk exposure. The risk involved is directly related to the fulfilment of outstanding obligations by the Group's counterparties. The Group maintains an awareness of potential losses relating to credit risk exposure and chooses its counterparties based on business experience and acceptable credit ratings.

Industry-related risk factors

At group and subsidiary levels, management monitors and assesses the airline industry's risk exposure, which has historically posed uncertainty, even in normal operating conditions. A part of the Company's culture stems from its long history, including a general recognition of the value of learning from past experience. Yet, in addition to the retrospective view, management systematically focuses attention on potential threats from a prospective viewpoint, as the environment is extremely changeable. The Group operates and thrives in well-established and defined markets which, as such, can be regarded as valuable intangible assets that require attention. Icelandair's credibility and reputation are crucial for its market status and growth. But the markets are also sensitive to external factors, such as the macroeconomic elements governing aggregate demand. An economic downturn will usually reduce the general purchasing power of potential customers and thereby the demand for air travel. Airlines are prone to even greater vulnerability when it comes to other types of shocks which are more sudden and forceful. Eruptions in recent years have caused costly and unanticipated threats of disruptions. Terrorist incidents and pandemics are also examples of events which need to be considered at all times. Factors that can be analysed and monitored with respect to reasonable risk of occurrence and impact call for close monitoring and readily available contingency plans. The ash cloud experience of Eyjafjallajökull Glacier in 2010 and Grímsvötn in 2011 put the contingency planning and operational flexibility of Icelandair Group to the test and they proved successful. This experience benefits the Group now in light of the current Holuhraun eruption and geological unrest in Bárðarbunga Glacier, which calls for constant monitoring and scenario analysis. The Company owes its adaptive potential and flexibility of operations chiefly to its capable human resources, contingency policies and economies of scale. The quality of the Company's responsive processes enables us to cope with other adverse circumstances and industry factors, such as seasonality, competition, insurance and new taxes.

Operational risk

The Group distinguishes between industry-related risks and those which expose the subsidiaries at individual company level. Embedded in the Group's operations is a natural spread of business risk, not only in terms of market diversification but also between the subsidiary business models themselves. This dispersion of interests has delivered rewards during periods of economic turbulence. Methods of coping with threats of disruptions and disturbances are also decentralized when it comes to operational hazards. Again, the long and successful history of Icelandair Group and its companies is a valuable asset, which serves both as the foundation and the benchmark for many of the policies and contingency plans used across the Group. The Group's computer and communication systems are crucial for sales and market activities, but also for undisrupted internal operations. Equipment maintenance is needed to guarantee airworthiness. Third-party services may become bottlenecks in the production chain, whether in catering, ground services or flight control. Human resources need to be managed, labour disputes resolved and work stoppages prevented. Wage negotiations were extensive in 2014 involving pilots, cabin crew and flight mechanics. These were favourably resolved after extensive efforts on both sides. Management constantly evaluates the risks involved and the potential consequences of individual events. Scenarios are projected, charted and contemplated and action plans launched based on possible outcomes, where collaboration is maintained between the Group and its individual companies.

Enterprise risk management

Risk management needs access to a secure and steady flow of information about all enterprise-related risks at the Group level and thus requires centralised mapping and detailed registration of risk items and their estimated inherent financial value and potential consequences. The Group's Risk Management Committee has focused on enterprise-related risk assessment in collaboration with Internal Audit and concentrated on aligning risk records across all subsidiaries for consistency and compliance. The key objective of Enterprise Risk Management is to enhance motivation in risk analysis and improve risk awareness, standardise the quantification of risk and establish the Company culture that is needed to promote everyday risk awareness and risk-reduction measures. Cash-flow stress testing is now performed with enterprise risk inputs by simulating events and scenarios induced by the factors defined in the risk registry. Although based on sensitive and qualitative assumptions, this practice has the merit of shedding light on the possible operational and financial consequences of external and internal disturbances. Quarterly results are submitted to the Internal Audit Committee for evaluation and support.

05

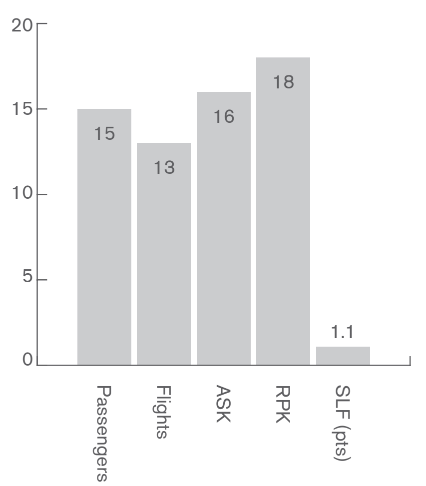
JÖKULSÁRLÓN | 64°2'38" N 16°10'32" W

Nature on the rocks with a twist.

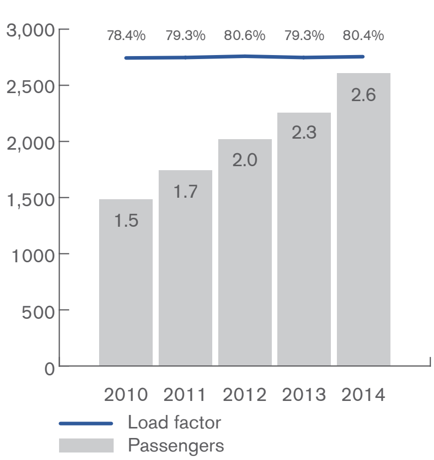
International Route Network

The business concept behind Icelandair Group's largest subsidiary, Icelandair, is based on Iceland's advantageous geographic position on the flight routes between northern Europe and North America, making it an ideal central point for an extensive international hub-and spoke airline network spanning the distance between both continents. In a typical element of Icelandair's Route Network, an aircraft will take off from Keflavik Airport in the morning and fly to Europe. It will then return later in the day and continue westward to North America to return to Iceland on the morning after.

Traffic Data | YOY %



Number of passengers (millions) and load factor | 2010–2014



Three different and independent passenger markets served

The Icelandair's Route Network serves three different and independent passenger markets: the Icelandic domestic market, i.e. the FROM market, the tourist market with Iceland as a destination, i.e. the TO-market, and the international market between Europe and North America, i.e. the VIA market. Serving these three markets with the same aircraft enables the Company to offer a higher flight frequency and a greater variety of destinations than the markets to and from Iceland alone would allow. Of the three markets, the VIA market is the largest and has been the main driving force of the growth of the Route Network in recent years. Since 2010 the proportion of VIA passengers has grown from 38% to 48% of the total passenger numbers in 2014.

Continued growth of the Route Network

Icelandair's flight schedule for 2015 will be the largest in the Company's history, growing by 14% from the 2014 schedule. Two new destinations are being added to the Route Network: Portland, Oregon, on the American West Coast, and Birmingham in the United Kingdom. In addition, the frequency of flights to various cities in North America and Europe will be increased. Fifteen weekly flights will be added to both North America and Europe, or 30 flights in total. The number of weekly departures from Keflavik will increase from 254 to 284 over next summer's high season. The new destinations will provide excellent opportunities to strengthen the Route Network still further. Flights to St. Petersburg, however, will be discontinued. The number of passengers in 2015 is projected at close to 3 million, as compared to 2.6 million in 2014. A total of 24 Boeing 757 aircraft will be used to serve the Company's passenger routes next summer, three more than in 2014.

Increased connectivity in a growing network

In 2015 the Route Network will connect 25 European cities with 14 North American cities through the hub in Iceland during the high season. The 39 destinations offer our customers 347 connection options, which corresponds to a connectivity multiple of 8.9 times the number of destinations. In 1990 the Route Network comprised 12 destinations with the option of 39 connections for our customers, representing a connectivity multiple of 3.25 relative to each destination. This comparison illustrates the exponential increase in the Network's connectivity.

Number of destinations and flight frequency of the Route Network increasing

When a new flight schedule is announced for the coming year the new destinations will usually get the most attention, but in fact the greatest change from 2014 to 2015 will lie in the greater frequency of flights to and from the current destinations. As an example of the extended reach of the Route Network, year-round flights will now be offered to eight cities in North America, up from four cities two years ago, and daily flights will be offered all year to seven European cities, up from four cities two years ago.

The Route Network

Iceland's uniquely central location between Europe and North America is the key to our hub-and-spoke network.

In 2015 the Route Network will connect 25 European cities with 14 North American cities through the Company's hub. The number of passengers in 2015 is projected at about 3 million, with 24 Boeing 757 aircraft serving the Route Network.

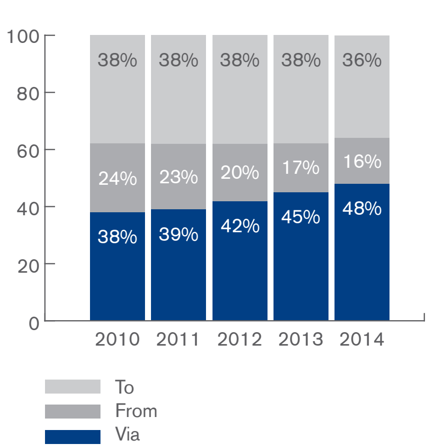
24-hour hub and spoke concept at Keflavik Airport

The heart of the Route Network is the 24-hour hub at Keflavik Airport. In the morning Icelandair's aircraft take off for all the destinations in the East. They reach Europe around midday and start the return flight early in the afternoon. Because of the 2-hour time difference between Iceland and most of Europe, the fleet is typically back in Keflavik at around midday, Icelandic time. The North America operation begins toward late afternoon and the fleet arrives in the U.S. and Canada in the early evening and returns to Keflavik early in the morning of the next day, just in time to depart again for Europe.

Establishment of a second connecting bank

The main focus to date has been on connecting flights through the hub at Keflavik, with morning flights to European cities and afternoon flights to North America. In recent years, however, a second connecting bank has been set up, with departures from Keflavik just before noon. In 2014 there were two flights daily through this second bank to North America and four flights to Europe. A third flight to North America will be added in 2015, as well as a fifth flight to Europe. The expansion through a second bank gives the option of two separate departure times per day to certain destinations, providing extra support for the main connection bank in the morning.

Passenger mix | 2010–2014



Two thirds of the seat capacity on flights to Europe

Almost two thirds of the seat capacity in the Route Network is on flights to Europe, with the remaining capacity deployed on North American routes. The United States is Icelandair's largest single destination country, while its European network focuses mainly on Scandinavia and Northern Europe, with the United Kingdom as the Company's second largest destination country. Daily year-round frequency is offered on 10 out of 39 routes. The Company offers seven routes with a frequency of double daily flights or more during the peak season.

Single fleet of Boeing 757s

Iceland is situated on the busiest transatlantic flight paths connecting North-America and Europe. Flights from Iceland to Europe are between 3 and 4 hours long, and flights to North America take between 5 and 8 hours which enables the use of narrow-body Boeing 757 aircraft in the entire Route Network. In 2014 the fleet comprised a total of 21 Boeing 757 aircraft, the majority configured with 183 seats. Three 757s will be added to the fleet in 2015, bringing the total number of aircraft in the Network to 24. The Company's aircraft have three classes: a business class, economy comfort and economy class. The fleet is equipped with personal in-flight entertainment system and Icelandair has started to offer on-board WiFi connections on its routes across the North Atlantic.

New aircraft type introduced in 2018

The Company has ordered sixteen 737 Boeing MAX8 and 737 Boeing MAX9 aircraft, with an option to buy an additional eight aircraft. Delivery of the first aircraft is scheduled for early 2018. The order involves nine 737 MAX8 aircraft, with a seating capacity of 153 passengers, and seven 737 MAX9 aircraft, with a seating capacity of 172 passengers. A mixed fleet of Boeing 757s and Boeing 737 MAX aircraft fits well into Icelandair's Route Network, as Europe and North America are within the reach of both aircraft. The new aircraft will be an excellent addition to the fleet and increase both flexibility and capacity for growth through added frequency and new destinations.

Offices in all key markets

International marketing and sales activities are organised through Icelandair's offices in its key markets: North America, Scandinavia, Continental Europe, the United Kingdom and Iceland, the last being the location of the Company's headquarters. In addition, the Company has sales agents in large markets outside the core network, such as Asia. Extensive efforts are being made to promote Iceland as a tourist destination and to brand Icelandair as a stimulating and uniquely Icelandic travel experience.

78 years of operations

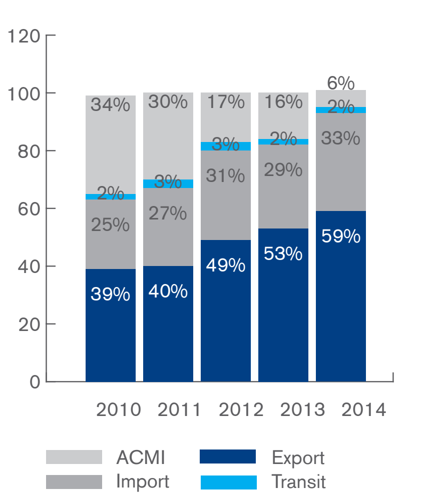
The strategy of Icelandair is to use the efficiency and flexibility of its operation to be the leading airline for travel to and from Iceland as well as a distinctive and exciting alternative for air travel across the North Atlantic. The mission is to operate a first-rate airline and to maintain a reliable quality service through the experience and knowledge gained from 78 years of operation.

- Our strategy is regularly and continually tested in order to enable Icelandair Group to fully understand the competitive market in which we operate and to take advantage of any hidden opportunities that may exist and any new opportunities that may arise.

Cargo Operation

Icelandair Group's cargo operation focuses on air-freight services to and from Iceland by leveraging the Group's strong international Route Network, which comprises Icelandair's passenger routes combined with scheduled air cargo flights to and from North America and Europe.

Revenue split | 2010–2014



Iceland's largest air cargo operator

The market area served by Icelandair Group's cargo operation is based on the Group's international Route Network. In addition, two B757-200 cargo aircraft are engaged in scheduled flights to destinations in Europe and the United States. A total of 40 destinations were on offer in 2014, with no major changes planned in 2015.

Collaboration with overland haulage companies

Extensive collaboration with overland haulage companies in Europe and North America enables services to and from all the principal cities in these market regions. Icelandair Group also co-operates with a number of other air carriers to offer continued flights to more distant markets, including Asia.

Offices in New York and Liege

The cargo operation has offices in New York and Liege in Belgium, which are responsible respectively for business in North America and Central Europe. In addition, cargo operation has agencies in all of Iceland's principal market areas in Europe, America and Asia.

ACMI operations discontinued in 2015

The cargo operation has also operated aircraft in ACMI projects for courier companies such as TNT and DHL. In recent years this operation has been challenging due to the economic difficulties in Europe. It was therefore decided to downscale these operations and in the past two years two aircraft have been withdrawn from these services and returned to their owners. The last aircraft servicing ACMI projects was returned in September 2014.

Fresh fish the most important export product

The Group's cargo operation has been growing in recent years. Carried freight measured in freight ton kilometres (FTK) amounted to 97.7 million FTKs in 2014, up by 3% from the preceding year. The total increase from 2010 is 34%. Fresh fish has been the most important product for the export part of the operation, and in particular the volume to America has been increasing. Imports to Iceland showed the greatest growth in 2014 since the economic crisis in 2008. Live lobster is the principal product carried between America and Europe.

Favourable future prospects

Icelandair Group's cargo network places the Icelandic fish industry in a unique position to distribute its products, which in turn will continue to strengthen the market position of the Group's cargo operation for exports. Fresh fish will remain the fundamental product for export going forward, as it has been in recent years. After the strong increase in exports over the last years, particularly to North America, a slower increase is anticipated in 2015. The main reason is the reduction in Icelandic Haddock quotas in 2015. The outlook for imports is better for 2015 than in any year since 2008, as imports are projected to increase in line with improving economic conditions in Iceland. A significant increase in imports to Iceland was observed in the second half of 2014, and this trend is expected to continue in 2015.

Aircraft Leasing

Icelandair Group offers capacity solutions to international passenger airlines and tour operators under the Loftleidir-Icelandic brand. Launched as a marketing vehicle for the Group's international Aircraft, Crew, Maintenance and Insurance (ACMI) and charter services, Loftleidir-Icelandic has narrowed its focus to leverage its expertise as a capacity solution provider concentrating mainly on Aircraft and Maintenance (AM) projects and consulting services.

Fleet

The company operated at the end of 2014 seven Boeing single aisle aircraft. Two B757 200s, two B767 300s, two B737 800s and one B737 700.

Long-term contracts expired in 2014

In January a contract with Santa Barbara Airlines in Venezuela expired after nine years of co-operation. Also, a seven-year collaboration with Yakutia Air Company came to an end in early spring 2014, when the third and last Boeing 757 was returned from the Republic of Sakha.

New contracts secured

A five-year AM contract, starting in June 2014, was secured with the French all-business class operator LaCompagnie for scheduled flights between Paris and New York.

In October a business relationship with Luxury Travel Experts Abercrombie & Kent in the US was revived when Icelandair Group undertook the operation of the company's first VIP Private Jet tour in six years. The service features a newly fitted VIP aircraft incorporating 50 lie-flat adjustable sleeper seats.

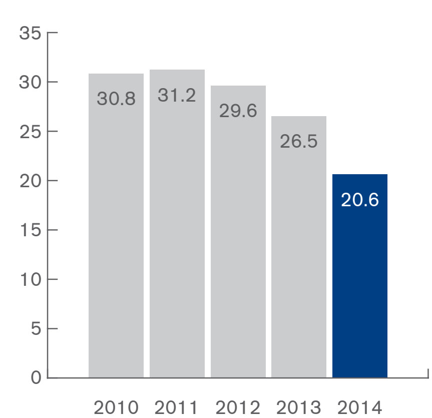
In December 2014 a contract was signed on the launch of Icelandair Group's first full charter operation in eight years, with flights out of Boston in the United States to Cancun, Mexico, and Punta Cana in the Dominican Republic in the service of Apple Vacations, the United States' largest tour operator.

As before, Air Niugini in Papua New Guinea will continue as one of the Group's capacity solutions customers, with five aircraft on long-term AM contracts.

Continued emphasis on the AM product

The overall outlook in the aircraft leasing market continues to improve. The demand for smaller single-aisle aircraft, mainly A320s and B737 NGs, is strong, as market availability remains limited. Although appetite for the B757 on the wet lease market is limited, the type is still in high demand on the dry lease market. At the same time the surplus availability of wide body aircraft continues, especially of the B767 type, which again is reflected in the wet lease and charter markets, where the A330 seems to be the preferred option. This trend is expected to continue in the near future. Icelandair Group's aircraft leasing operation will continue to focus on the Group's AM product while maintaining its marketing efforts in the VIP, ACMI & Full Charter markets.

Number of sold block hours (thousands) | 2010–2014



Hotels and Hospitality

Icelandair Group's hotel operations provide hospitality services through a cohesive mix of international and local brands. The Icelandair Hotel brand fuses traditional hotel hospitality with innovative services to keep up with the trends and requirements of the modern traveller's lifestyle.

Authentic Icelandic experience
The vision of the Group's hotel operations is to create an authentic Icelandic experience for visiting tourists. The focus is on leveraging the unique qualities of Iceland as a tourist destination to add value to Iceland and to support the Group's other operations.

Principal markets linked to the Route Network
Although guests using Icelandair Group's hotels come from all over the world, the principal targeted markets are linked to the Group's international Route Network. The ongoing increase in the number of flights on existing routes and new N-America gateways provide ample opportunities for further growth for the hotels. Marketing efforts in 2015 will focus both on existing and new gateways.

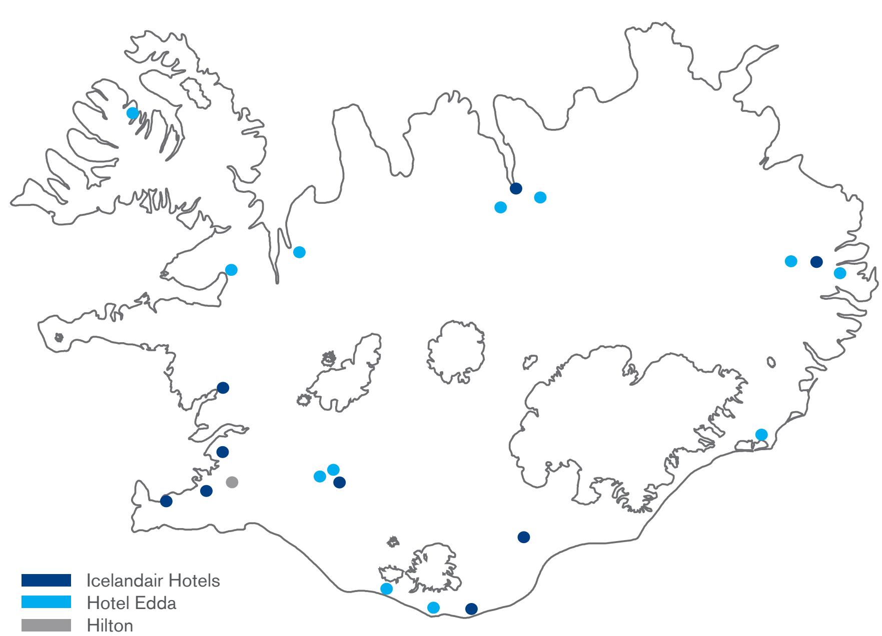
Three hotel brands operated
Icelandair Hotels operates a chain of all-year hotels under the domestic Icelandair Hotels brand and under the international brand Hilton. In addition the Icelandair Hotels operate the summer hotels Edda.

Supporting value creation for Icelandair Group
It is the strategic goal of the hotel operation to support value creation for Icelandair Group through a positive perception of Iceland as a destination, as the Group collectively aims for a long term build-up of "higher spending" segments visiting Iceland year-round.

Increased occupancy and average room rate in 2014
The favourable results of recent years in terms of increased occupancy and average room rates were surpassed in 2014. The continued success of the newest property, Icelandair Hotel Reykjavik Marina, which opened in April 2012, was one of the year's highlights, as well as the ongoing development of additional deluxe rooms and public areas scheduled for opening in the spring of 2015. A new franchised Icelandair Hotel opened in May, Icelandair Hotel Vík which has been well received. Another focal point was the planning and design work on new properties scheduled for launch in 2016.

Improved processes in 2014
Ongoing development and further improvements of the company's infrastructure and technical solutions made their mark on the year's operations, as well as successful improvements in the online appearance and booking interface of all three hotel brands.

Location of our hotels | 2010–2014



In-house education and training centre

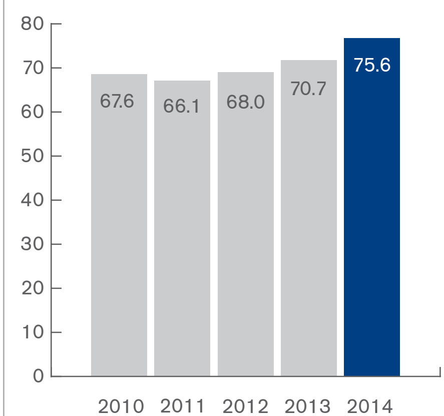
In 2014 attention was focused on further developing Icelandair Group's own in-house education and training centre. The purpose of the centre remains to attract future culinary and front-line candidates in order to build up and improve the local hospitality infrastructure, as well as to support Icelandair Group's own operations in line with the increasing number of hotel rooms and expanded food and beverage services offered by the Company.

Ongoing increase in bookings and revenues foreseen in 2015

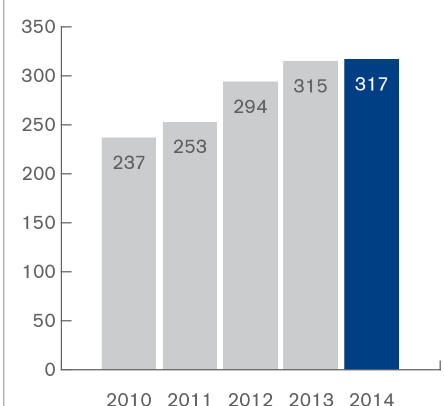
In addition to taking advantage of the abundant opportunities for further growth for Icelandair Group's hotels arising out of both the existing and new gateways of the international Route Network, other main projects will include the completion of improved facilities at Icelandair Hotel Reykjavik Marina, as well as the preparation and design of two new downtown hotels, both of a higher quality than available before in Reykjavik. In addition to work on renovating our properties, efforts will continue to improve booking procedures, increase online visibility and enhance the Group's brand strength.

While the expanded flight schedule of our international Route Network will open new markets, resulting in better hotel room occupancy, the ongoing construction of new hotels in Iceland will result in competitive downward pressure on average prices and could result in a more challenging environment. Nevertheless, the focus of Icelandair Group's hotel operations remains clear: to continue leading the way as the outstanding provider of an authentic Icelandic experience at all our properties.

Occupancy % | 2010–2014



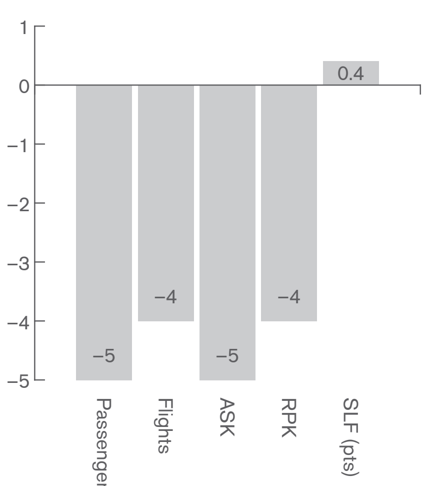
Available hotel room nights (thousand) | 2010–2014



Regional Airline Operations

Icelandair Group's regional carrier, Air Iceland, offers domestic flights to four destinations in Iceland and four destinations in Greenland. The focus is on offering efficient and reliable air transport to improve the quality of life of people living in sparsely populated areas with limited options for short travel times to and from urban centres. Dependable regional flight services also make it possible for a number of business undertakings and public agencies to operate in an efficient manner. Co-operation with other airlines enables interregional connections, both domestically in Iceland and Greenland and to the Faroe Islands.

Traffic Data | YOY %



The roots lay back to the dawn of aviation in Iceland

Icelandair Group's regional airline operations have strong roots that extend back to the dawn of aviation in Iceland. The aim of the Group's regional services is to operate an extensive and flexible domestic flight schedule in Iceland and the West Nordic countries. In the course of our decades of domestic and regional air services, Icelanders have relied on our efforts to enable close links between friends and families, swift communications between businesses and just-in-time deliveries of goods and supplies. Tourists in Iceland have also appreciated the opportunities afforded by Air Iceland for quick transport to remote areas.

Fleet

The Group's regional fleet comprises five Fokker 50 and two Dash-8 aircraft.

Domestic flights are operated on Fokker 50 aircraft, which have a long-standing reputation for dependability on domestic routes in Iceland.

Regional flights to Greenland are operated on Dash 8-200 aircraft. These aircraft are particularly suitable for this service as they can cope with quite short runways. To give an example, they can take off with a full load from runways approximately 800 metres long while withstanding stronger crosswinds than other comparable aircraft. They can also carry more freight than other aircraft of similar size and they can be specifically configured to carry cargo alone.

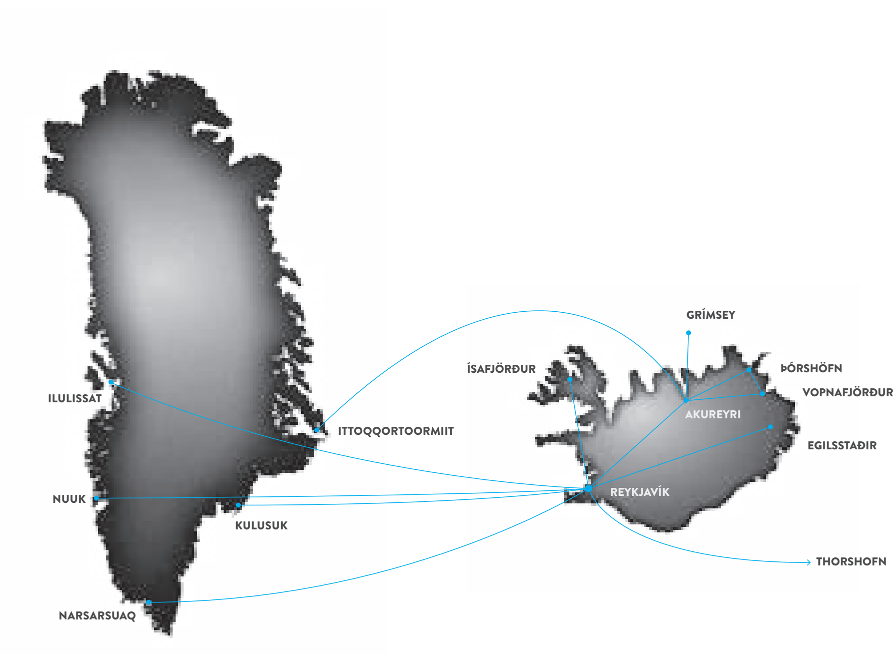
Growth of tourism in Iceland stimulates demand

Icelandair Group's regional operations have benefitted from the growth in tourist arrivals in Iceland over the last five years. Product development has increasingly been focused on foreign tourists with marketing efforts concentrated on the offer of a wide variety of day tours and multi-day tours combining domestic and regional flights. The relative proportion of foreign tourists utilising the domestic network stands at around 10% of total passenger numbers and is Air Iceland's fastest growing market segment.

Double digits growth on Greenland flights

On Greenland flights growth in terms of percentage has been in the double digits over the last five years, and this trend is expected to continue in 2015. New product development, offering varied and attractive packages, lies at the heart of the marketing efforts in the Greenland market.

Route Map | Regional Airline Operations



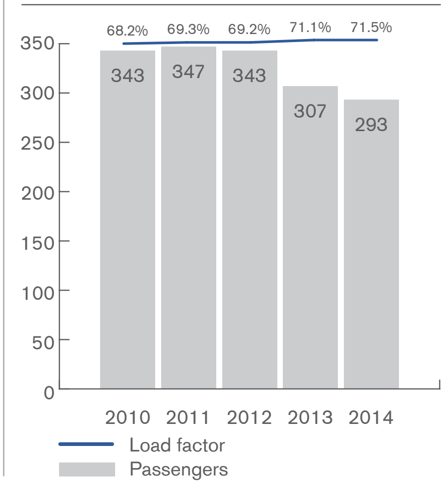
Improving outlook in the domestic market

The Air Iceland's domestic operation has historically shown a strong correlation with the underlying performance of the local economy in Iceland. Most economic forecasts assume continued growth in Icelandic GDP with increased purchasing power and investment capacity, which should be reflected in growing demand for domestic flight services. However, future prospects will also depend on government policy regarding public levies on air travel. The current government is seeking ways to reduce the tax burden on domestic air fares, but it remains to be seen whether any actual and significant changes are made.

Greenland growing as a tourist destination

Although mining and oil exploration in Greenland are currently at a low, the demand for Greenland as a tourist destination is growing and the number of passengers on routes to and from Greenland is expected to increase in 2015 from 2014 as has increased for the last half a decade. Air Iceland's focus on the tourist market to Greenland will be further extended as the demand for travel to Greenland continues to grow from both established and new markets.

Number of passengers (thousands) and load factor | 2010–2014



06 BÚÐIR IN SNÆFELLSNES | 64°49'17" N 23°22'45" W

The tangible energy of glacier Snæfellsjökull lends an aura of mystery to this place.

Icelandair Group and Society

Iceland: an island in the middle of the Atlantic Ocean, rich in natural wonders, culture and social values. Icelandair Group is a part of the Icelandic society. Every day we contribute to our society by creating value. Every day we strive to meet the needs of our customers. Icelandair Group is proud of its role in the Icelandic community and continues to seek new opportunities to expand its ties to society at large. That is how Icelandair Group energises the power of the Icelandic tourism industry for the benefit of Iceland as a nation.

Focus elements of our stakeholder model

We focus on creating sustainable value for our stakeholders by integrating into our business model a wide range of efforts to ensure our social responsibility.

- **Employees and Governance:** Exemplary corporate governance and commitment to our employees with extensive programmes for human resource development.
- **Environment:** Minimize our impact on the environment by setting measurable targets, raising awareness and benchmarking our performance to do better than before.
- **Society:** Co-operate with society and ensure that the impact of our operations is beneficial through direct contributions and positive engagement with society at large

We believe in stakeholder engagement. We believe in matching ourselves against other international airlines and tourism companies, identifying where the Group stands in comparison with its competitors and finding where improvements can be made. Finally, we believe in regularly reviewing our sustainability initiatives and maintaining an open dialogue with our employees.

It is our firm belief that a clear and concise social responsibility strategy, when successfully implemented, will add value and have relevance for economic, environmental and social factors, for both Icelandair Group and for our key stakeholders.

Developing our sustainability strategy

It is important to bear in mind that our adherence to a sustainability strategy does not simply mean tweaking current initiatives that are already being successfully implemented; it means putting all our current activities and various initiatives into a coherent and comprehensive context that can be easily communicated and understood by stakeholders, and it means adding new priorities and setting new measurable targets. It means educating our employees, engaging them and empowering them to develop new initiatives.

Formalising Icelandair Group's sustainability efforts in 2015 will give us a clearer vision of our current sustainability performance, allow us to identify areas that need further attention and enable clear communication of our efforts to customers, employees and society at large.

We are committed to continuous improvements. We see a coherent and well-implemented sustainability strategy for Icelandair Group as a means of deepening our understanding of the Company and the environment in which we operate, through:

- A clearer view of the Company's risks and opportunities when it comes to environmental and social factors;
- Clearer communication with internal and external stakeholders;
- Better coordination among the different subsidiaries of Icelandair Group when it comes to environmental and social risk.

At Icelandair Group, we believe that the implementation of a sustainability policy is most likely to be successful if the policy is directly linked to the company's business strategy. That is how we contribute best to our society.

Employees and Governance

Icelandair Group has enjoyed a steady and rewarding growth in recent years, and our employees have played an integral part in our success. Their quality, dedication and team spirit have repeatedly been put to the test and they have come through every time with flying colours. They possess a broad range of skills and knowledge, as required by the diverse nature of our operations, which benefits the Group as a whole. We strive to provide our employees with attractive and challenging opportunities so that we can remain successful and continue to grow.

Exemplary in corporate governance

The Iceland Chamber of Commerce, the Confederation of Icelandic Employers and the Centre for Corporate Governance of the University of Iceland recognised Icelandair Group as "Exemplary in Corporate Governance" in 2013. Icelandair Group was the first listed company in Iceland to receive the recognition.

Icelandair Group holds the view that functional Corporate Governance principles are essential to assure shareholders and other stakeholders that the Company is doing its best to ensure sound and effective control of its affairs and a high level of business ethics.

Embracing good Corporate Governance will, in the long run, build a solid Company with satisfactory profits for shareholders on their investment. Corporate Governance serves to ensure an open and transparent relationship between the Company's management, its Board of Directors, its shareholders and other stakeholders.

Employees

Over the last five years the number of employees at Icelandair Group has grown by more than forty percent. Such rapid growth can cause some strain, and during this time we have also had to face disruptions to our services caused by natural disasters. This has tested the mettle of our employees, both old and new, and they have responded admirably. They have displayed resilience and energy, together with initiative and flexibility and great team spirit, thereby underlining their commitment to the Company. This commitment cuts both ways.

We always try to maintain the strong culture that is needed to link different corporate units and employees and instill the team spirit we originally fostered in our base in Iceland. We make every effort to bring all our employees, from all companies within the Group, in Iceland and abroad, into our family.

Icelandair Group employees, full time equivalents (FTEs), by company 2010–2014:

	2010	2011	2012	2013	2014
Icelandair	981	1,179	1,236	1,387	1,529
IGS	354	386	425	469	544
Icelandair Cargo	37	44	47	49	49
Loftleidir	11	11	11	11	11
Air Iceland	225	224	224	230	221
Icelandair Hotels	234	313	384	468	495
Iceland Travel	71	76	64	94	115
Vita	-	-	21	19	18
Fjárvakur - Icelandair Shared Services	101	105	107	109	115
Parent company	14	13	13	13	12
Total	**2,028**	**2,350**	**2,532**	**2,850**	**3,109**

Employees and Governance, continued:

Recruitment

Icelandair Group is one of Iceland's largest private employers and the de facto flagship carrier of Iceland. As such, we are able to recruit well-qualified personnel from a large local pool of talented and dedicated individuals who are eager to work for the Company. We can offer a wide range of jobs for highly trained professionals at competitive salaries in an international working environment.

We have designed a thorough and tailored recruitment process to ensure that we select the people best suited for each specific type of job, not only based on professional qualifications, but also on our perception of how they will fit into our results-driven corporate culture.

Because of the seasonality of our business we need to take on over 1,100 extra staff over the high tourist season in Iceland. Many return to work for us year after year and later join us as full-time employees. As they acquire knowledge of our business they gain faith in their work, loyalty to the Company and pride in its success.

Professional development

The professional development of our employees is a subject close to our heart. We want to employ people who find satisfaction in developing their skills, adding to their knowledge, and then putting these skills and knowledge to meaningful use in their work. We provide our employees with a variety of training opportunities and courses that suit their needs, because we want to make the best use of their talents. This fits well with another aspect of our policy, which is to recruit a large part of our management team from within the Company. This ensures that our managers are well versed in our culture and have a thorough knowledge of the Company from the outset. Over the last three years more than 70% of new managers have been promoted from within our own ranks.

Communication

We believe it is necessary to keep our employees constantly informed with timely and accurate reports on Company affairs. This is especially important, because our operations are so diverse and dispersed over so many countries. Information is shared through newsletters, employee meetings and over the Company intranet, MyWork, which also acts as a conduit for sharing work-related knowledge among employees.

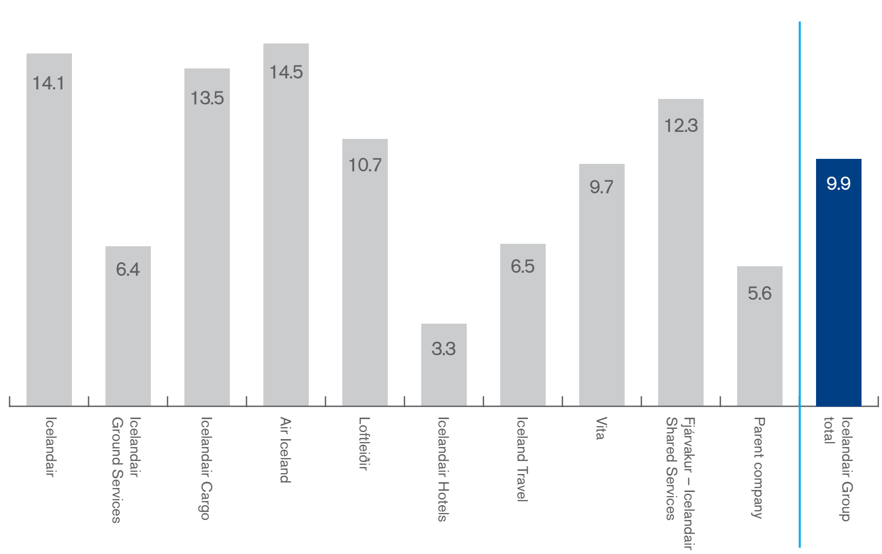
In MyWork we have created a way to store the reservoir of experience and knowledge possessed by our employees and channel this experience efficiently so that those who need it can tap into it at will. MyWork is steadily being enhanced and improved. Giving employees easy access to the information they need, when they need it, improves efficiency and leads to greater job satisfaction, saving both time and money.

Through exchanges of this kind we are able to build trust between employees and management, which in turn is the basis for achieving optimum results. All of this serves to keep our employees committed and maintain a team spirit within the Company.

Full time equivalents (FTEs) | by company

	Jan. 2014	Jul. 2014
Icelandair	1,333	1,764
IGS	411	729
Icelandair Cargo	46	53
Loftleidir	11	11
Air Iceland	210	256
Icelandair Hotels	411	705
Iceland Travel	97	120
Vita	17	18
Fjárvakur - Icelandair Shared Services	113	132
Parent company	12	12
Total	**2,661**	**3,800**

Average job tenure | by company



Human resources strategy

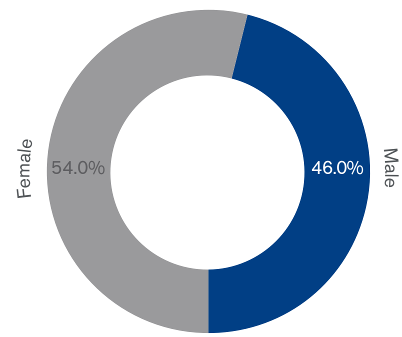
Icelandair Group seeks to attract qualified employees who can help the Company meet the challenges of the future while upholding the standards that have served us so well in the past. In order to attract ambitious and qualified people we strive to maintain an attractive workplace that is challenging and demanding, but at the same time welcoming and satisfying, so that we are always able to select the best person for every job.

All employees are required to respect our non-discrimination policy and conduct themselves accordingly. Our HR strategy also emphasises equality and embraces diversity in our workforce. We have put in place detailed action plans to ensure that our goals are met. We encourage and assist our employees in maintaining their strengths as they acquire more skills and knowledge through training and experience. We will also ensure that they are given equal opportunities to further their careers. Above all, we will make sure that all our employees feel they are part of a team.

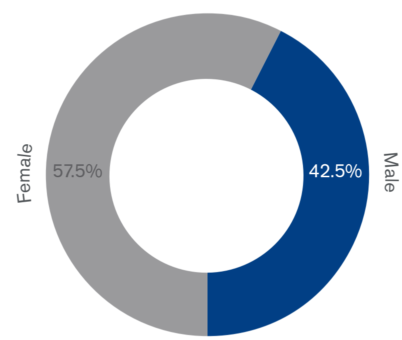
Corporate culture

The corporate culture of Icelandair Group originates in our awareness of being a big player in a small market and, at the same time, a small but unique player on the global scale. Our strengths have been flexibility, efficiency, responsiveness, drive and quick decision-making. Our culture is characterised by a strong team spirit and a can-do attitude, which enables all our employees to flourish and achieve their highest potential. We know that the Company is engaged in providing an essential service, where every employee is important and every customer is valuable. We need to be at our best so that we may serve our customers best.

Male / female ratio Icelandair Group
January 2014



Male / female ratio Icelandair Group
July 2014



Environment

Icelandair Group is an environmentally conscious company, dedicated to minimising the impact of its operations on the planet's climate and the global environment. The Company contributes to a sustainable future by designing and implementing innovative solutions and initiatives to achieve its goals.

Icelandair Group is going green

Icelandair Group's environmental impact is not limited to flight operations. It also involves ground facilities, offices and maintenance areas. Our goal is to maximise the use of green energy and minimise waste in all operations by adopting sustainable solutions.

In order to achieve this goal, Icelandair Group is preparing to obtain ISO-14001 Environmental Management System certification for all Icelandair Group companies by 2016. We have already achieved ISO-14001 certification for Icelandair Hotels and Icelandair Ground Services.

Icelandair Group is committed to implementing programmes of continuing environmental education for its staff and informing its customers of the importance of environmental awareness. In this way we seek to contribute to a successful future for our Company, as well as for the rest of the world.

Environmental Policy

Icelandair Group's Environmental Policy describes our approaches to protecting and preserving the environment. All Company employees are responsible for ensuring compliance with Company policy. Management at all Company subsidiaries and entities are adopting guidelines and procedures to comply with the following environmental statement.

The Company intends to:

- Comply with all environmental laws and regulations.
- Obtain ISO-14001 EMS certification for all Icelandair Group companies by 2016.
- Regularly communicate environmental awareness matters to employees, customers, suppliers and the public.
- Protect the environment by adopting sustainable business practices, technologies and procedures that maximise the use of green energy, minimise pollution and greenhouse gas emissions and manage waste.
- Report publicly on the Company's environmental performance, including greenhouse gas emissions.
- Continuously improve the Company's environmental performance in compliance with ISO-14001 by setting specific environmental improvement targets, monitoring progress and communicating results internally.
- Conduct regular audits and reviews to assess the environmental programme and facilitate preventive and corrective measures.
- Provide all employees with appropriate training in environmental awareness and in complying with environmental rules and regulations in our operations to minimise our impact on the environment.
- Require every employee to comply with this environmental statement and with procedures relating to environmental sustainability.
- Encourage employees to identify environmentally friendly methods to enhance our daily operations.

Environmental awareness

Icelandair Group is committed to increasing the environmental awareness of its staff for the sake of future generations. All employees are familiarised with the environmental rules and regulations that apply to our operations to minimise our impact on the environment. We also communicate environmental awareness to our customers, suppliers and the general public.

Icelandair Group has already implemented an environmental awareness training program designed to highlight our planet's ecosystems, the sensitivity of groundwater to pollution, the risks of greenhouse gas emissions and the importance of recycling and re-using materials to preserve Earth's resources.

Protecting the atmosphere and maximising use of green energy

Climate change is one of the main challenges faced by Mankind. Industry, science, politics and the public need to reduce greenhouse gas emissions and promote the efficient use of natural resources. Icelandair Group sees climate preservation as an important mission due to the impact of its business on Earth's climate and seeks to reduce greenhouse gas emissions and maximise the use of green energy in its fleet.

To this end Icelandair Group has established numerous programmes to maximise fuel efficiency and invested in new technology that reduces fuel consumption.

Fuel consumption and fuel efficiency

Recognising the importance of conserving fuel and minimising CO_2 emissions, Icelandair Group monitors and evaluates all new ideas and solutions in this field, and all departments participate in this activity. The main goal of the Icelandair Fuel Management Committee is to reduce fuel burn and thereby CO_2 emissions. During the past few years numerous changes have been made to both the Company's operations and its aircraft. For example, most aircraft are now fitted with winglets that reduce fuel burn. Icelandair constantly pursues new ways of improving fuel burn in Icelandair operations by analysing every aspect of all flights and flight planning. In 2014 fuel burn was 3.83 litres per 100 RPK (revenue passenger kilometre), as compared to 3.86 litres per 100 RPK in 2013, 3.81 litres in 2012, 3.9 litres in 2011 and 4.0 litres in 2010.

Aircraft noise reduction

International requirements in this field are laid down in ICAO Annex 16, “Environmental Protection”, Vol. I, which prescribes certain maximum noise levels for aircraft at three designated noise-measuring points. All aircraft operated by Icelandair have since October 1990 fully complied with the most stringent international requirements (as laid down in ICAO Annex 16, Vol. I). In addition, Icelandair strives to keep noise at a minimum by using noise abatement procedures.

Aircraft engine emissions

According to ICAO Annex 16, “Environmental Protection”, Vol. II, unburned hydrocarbons (HC), carbon monoxide (CO), oxides of nitrogen (NOx) and smoke emitted by aircraft engines must be controlled. All aircraft operated by Icelandair have since October 1990 fully complied with the most stringent requirements concerning aircraft engine emissions (as laid down in ICAO Annex 16, Vol. II).

Minimising waste and managing utilities

Icelandair Group acknowledges its responsibility to reduce the amount of waste resulting from its operations, whether aluminium tins, paper or used parts in maintenance areas. The Company has launched a Waste Management Programme to reduce, recycle and reuse materials across its organisation. Icelandair Group is committed to reviewing its processes and operations in order to identify possible ways to reduce unnecessary waste. The Company’s aircraft, ground facilities, offices and maintenance areas are dedicated to minimising its environmental footprint with regard to energy, materials and related emissions and waste. The Company focuses on best practices by implementing initiatives to minimise the use of resources and identify cost savings throughout the system.

The Waste Management Programme has been implemented throughout our entire organisation, and we will continue to promote, develop and encourage waste reduction, reuse and recycling on site in a systematic and cost-effective manner. We will use suitable regulated waste management contractors to secure safe management and handling of hazardous and non-hazardous waste sent off-site in accordance with best environmental practice. The Company’s goals are to reduce waste, reuse and recycle materials, conserve energy and reduce pollution and greenhouse gas emissions. Accordingly, our offices follow a “print-by-need” policy and they buy supplies manufactured from recycled material when available. Icelandair Group offices recycle paper, plastic, metal, batteries and used printer cartridges in an effort to reduce general waste.

Environmentally friendly purchasing

Icelandair Group will implement a purchasing policy under which we support suppliers that have adopted the best environmental practices. Our suppliers will be audited with regard to environmental awareness and the level of environmental control they have implemented in their operations in order to support our environmental policy. We will communicate information on environmental matters to our suppliers as necessary for the duration of our business relationships.

Environmentally friendly commuting

Icelandair Group views public transportation, carpooling, biking and telecommuting as means to save energy and reduce greenhouse gas emissions from employees’ travels to and from work. We pursue an environmentally sound commuting policy and encourage our employees to consider other options than drive-alone commuting in our effort to reduce greenhouse gas emissions and adopt more environmentally friendly practices. ■

Community

Icelandair Group is an integral part of Icelandic society. We are proud of our affiliations and effort we undertake each year to contribute to develop initiatives that further societal causes. By contributing and supporting our community, Icelandair Group has a positive impact on the wider society. In the end, the whole is larger than the sum of its parts. The various companies within Icelandair Group support a wide variety of community activities all year round. The main focus is on support for Icelandic sports, Icelandic music, the Icelandic tourist industry and the Special children travel fund.

Co-operation with Reykjavik University

RU is Iceland´s largest private university, a dynamic international university with over 3,000 students. We support and work alongside students and teachers at Reykjavik University on a wide range of annual projects. Knowledge sharing is key and each year we strive to engage new talent to work on various projects within our Company.

Special Children Travel Fund

The main objective of the Special Children Travel Fund (Vildarbörn) is to help children suffering from long-term illness or other difficult circumstances to see something of the world. The fund is supported both directly by Icelandair and through the generous gifts of our customers. In 2014 fifty children and their families, around 300 people in all, received travel grants from the fund to go on their “dream journey”. Since the fund was established eleven years ago, 471 families have been supported in this way. Vigdis Finnbogadottir, former President of Iceland, is the protector of the fund. For more details see www.vildarborn.is

The Icelandic Travel Fund

Icelandair Group is a leading shareholder in the Icelandic Travel Fund, an investment fund focused on new projects that increase the diversity of Icelandic tourism and strengthen its infrastructure. The fund’s main focus is on experience-based investments and on supporting the development of year round attractions for tourists and Icelanders alike. ITF is the leading investor in Fákasel, the Icelandic Horse Park, in Whales of Iceland, the largest whale exhibition in Europe and in Icecave, the largest man-made icecave in Europe, situated in the Langjökull glacier.

The National Olympic and Sports Association of Iceland

The National Olympic and Sports Association of Iceland (ISI) is the umbrella organisation of the entire sports movement in Iceland and the supreme authority in all amateur sports activities and associated volunteer work in Iceland under the Sports Act. ISI organises and oversees Iceland’s participation in the Olympic Games, Games of the Small States of Europe and other sports events held under the auspices of the International Olympic Committee (IOC). Icelandair has been a long-time supporter of ISI and is one of the four companies forming the ISI Olympic Family.

Icelandic Handball Federation

The Icelandic Handball Federation has sent its athletes across the world in team colours that prominently feature the Icelandic flag and the Icelandair Logo. Team handball is an extremely popular sport in Iceland, and Icelandic players and coaches have achieved outstanding results, both in Iceland and abroad. The Icelandic men’s team took the silver at the Beijing Olympics in 2008 and the bronze at the European Championship in Austria in 2010.

Iceland Football Association

The Iceland Football Association (KSI) was founded in 1947, and Icelandair has been a long-time faithful sponsor. The Icelandic national teams, the men’s and women’s A-teams and the U21, U19 and U17 teams, fly with Icelandair with the company’s logo on their travel attire.

Iceland Basketball Association

The Iceland Basketball Association is responsible for all basketball activities in Iceland, and Icelandair sponsors the Association and its affiliated basketball teams in competitions in Iceland and abroad. The national team will be playing in the EuroBasket championship in September 2015.

Icelandic Golf Association

Golf is an extremely popular sport in Iceland, and the Icelandic Golf Association is one of the largest sports associations in Iceland. Icelandair has actively supported the work of the Association in recent years, and Icelandic elite golfers have flown with Icelandair and borne the company’s logo on their competition attire. In 2012 Icelandair Group established a fund called Forskot along with the Golf Union of Iceland, and three other Icelandic companies. The objective of the fund is to support Icelandic professional and amateur golfers who aim to play golf at a world-class level.

Championship of the Icelandic Horse

Icelandair Cargo is the principal sponsor of the World Championship of the Icelandic Horse, which is held annually at various locations in Europe.

The Icelandic Cancer Society
The Icelandic Cancer Society has a remarkable history and has through the decades concentrated its engagement on prevention, education, research and patient services. Each year we donate a portion of the yearly income of the so called “Pink Suite” in Icelandair Hotel Reykjavik Natura in support for the ICS.

Iceland Sports Association for the Disabled
The Iceland Sports Association for the Disabled (IF) is the supreme authority in sports for the disabled under the auspices of the National and Olympic Sports Association of Iceland. IF organises and oversees Iceland’s participation in the Paralympics, the Special Olympics and other major sports events for disabled athletes. Icelandair has supported IF for 25 years and is one of the association’s five largest sponsors and partners.

Iceland Airwaves
Icelandair is the founder and main sponsor of Iceland Airwaves (or “Icelandair waves” as some of us like to spell it), a music festival held in October/November each year in Reykjavik. Iceland Airwaves is an annual music event that started in 1999 as a talent show for the benefit of foreign record company executives; since then Airwaves has grown and blossomed and is now an integral part of the cultural life of Reykjavík. The fruits of the festival’s labour have been ripening, and today many Icelandic artists, such as Sigur Ros, Of Monsters and Men, Ásgeir Trausti and others, have made their way to the international music scene. For more details see the festival website www.icelandairwaves.com.

Iceland Music Experiments
Icelandair is proud to offer young and talented musicians an opportunity to shine through Iceland Music Experiments (IME). IME is a musical event where young people make their musical début and get their first chance to step into the limelight and play their music. Icelandair rewards IME victors by offering them the opportunity to perform at the annual Iceland Airwaves festival.

Reykjavik Airbridge
Icelandair supports Icelandic musical talent beyond Iceland Airwaves. Through co-operation with the city of Reykjavik, Icelandair has set up a fund that helps Icelandic musicians to market themselves abroad. This allows them to tour and/or engage in other marketing activities outside Iceland.

Food and Fun
Food and Fun is an event which combines outstanding culinary skills, fresh natural ingredients, Icelandic outdoor adventure and the world-famous Reykjavik nightlife to create the ultimate recipe for fun. The core element of the festival involves world-acclaimed chefs who collaborate with Reykjavik’s best restaurants. Each chef is assigned to one of the participating restaurants, where they prepare a special menu, made exclusively with Icelandic ingredients. The menu is featured at all the restaurants for an entire week. In addition, the chefs themselves are on site for three nights during the festival week. Icelandair is the founder and owner of the Food and Fun event. More details online at www.foodandfun.is

Eyrarrósin
Air Iceland is the principal sponsor of Eyrarrós – a prize awarded annually to enterprises or persons who have made outstanding contributions to cultural activities in rural Iceland.

Save the Children Iceland
Icelandair Group is one of the main sponsors of Save the Children Iceland. The organisation is a part of the Save the Children International. It supports the human rights of children by being their advocate through educational activities, domestic and foreign projects and emergency relief. The organisation is guided in its work by the United Nations Convention on the Rights of the Child.

ICE-SAR – Slysavarnarfélagið Landsbjörg
Icelandair Group is since December 2014 one of the main sponsors of ICE-SAR, the Icelandic Search and Rescue operation. The Company’s objective is to provide support to enable the organisation to engage in efficient accident prevention and rescue efforts and to enhance the safety of tourists traveling in Iceland. The aim of the organisation is to minimise the frequency of travel accidents and reinforce the image of Iceland as a safe tourist destination by providing useful travel information and maintaining an effective safety net. The partnership will reinforce the already good work of ICE-SAR still further and will be an important factor in promoting safer tourism by various means, including the sponsorship and marketing of the SafeTravel.is website to tourists through Icelandair Group’s distribution channels. The sponsorship agreement also provides for additional support to ICE-SAR, an efficient all-volunteer organization, in its core field of search and rescue.

07

ELDHRAUN | 63°38'5" N 18°25'53" W

The Eldhraun lava field was formed when a row of craters, Lakagígar, wreaked havoc in the 18th century.

Endorsement and Statement by the Board of Directors and the CEO

Operations in the year 2014

The financial statements comprise the consolidated financial statements of Icelandair Group hf. (the "Company") and its subsidiaries together referred to as the "Group". The Group operates in the airline and tourism sectors with Iceland as a cornerstone of an international route network.

Profit for the year 2014 amounted to USD 66.5 million and total comprehensive income amounted to USD 38.0 million according to the consolidated statement of comprehensive income. Total equity at year end 2014 amounted to USD 365.1 million, including share capital of USD 40.6 million, according to the consolidated statement of financial position. Reference is made to the consolidated statement of changes in equity regarding information on changes in equity during the year.

The Board of Directors proposes a dividend payment to shareholders in 2015 of ISK 2.500 million, equal to USD 19.6 million, which represents 30% of profit for the year 2014.

Share capital and Articles of Association

The nominal value of the Company's issued share capital amounted to ISK 5.0 billion at year-end, of which the Company held treasury shares of ISK 25 million. The share capital is divided into shares of ISK 1, each with equal rights within a single class of shares listed on the Icelandic Stock Exchange (Nasdaq OMX Iceland). Companies can acquire and hold up to 10% of the nominal value of treasury shares according to the Icelandic Company's Act.

The Company's Board of Directors comprises five members elected at the annual general meeting for a term of one year. Those persons willing to stand for election must give formal notice thereof to the Board of Directors at least five days before the annual general meeting.

The Company's Articles of Association may only be amended at a legitimate shareholders' meeting, provided that amendments and their main aspects are clearly stated in the invitation to the meeting. A resolution will only be valid if it is approved by at least 2/3 of votes cast and is approved by shareholders controlling at least 2/3 of the share capital represented at the shareholders' meeting.

The number of shareholders at year end 2014 was 2,099 which is an increase of 266 during the year. At year end 10 largest shareholders were:,

Name	**Shares in ISK thousand**	**Shares in %**
Stefnir Sjóðir	891.163	17,82
Lífeyrissjóður verslunarmanna	729.136	14,58
Lífeyrissjóður starfsmanna ríkisins A deild og B deild	476.702	9,53
Gildi - lífeyrissjóður	265.042	5,30
Stapi lífeyrissjóður	179.977	3,60
Stafir lífeyrissjóður	179.615	3,59
Íslandssjóðir - IS Hlutabréfasjóður	163.489	3,27
Sameinaði lífeyrissjóðurinn	147.360	2,95
Íslandsbanki hf.	120.200	2,40
Landsbréf - Úrvalsbréf	117.636	2,35
	3.270.320	65,41
Other shareholders	1.704.220	34,08
Treasury shares	25.460	0,51
Total issued shares	5.000.000	100,00

Further information on matters related to share capital is disclosed in note 25. Additional information on shareholders are provided on the Company's website www.icelandairgroup.com.

Corporate Governance
The Group's management is of the opinion that practicing good Corporate Governance is vital for the existence of the Group and in the best interests of the shareholders, Group companies, employees and other stakeholders and will in the long run produce satisfactory profits on shareholders' investment.

The framework for Corporate Governance practices within the Group consists of the provisions of law, the parent company's Articles of Association, general securities regulations and the Icelandic Corporate Governance guidelines issued by the Iceland Chamber of Commerce, Nasdaq OMX Iceland and the Confederations of Icelandic Employers. Corporate Governance practices ensure open and transparent relationships between the Company´s management, its Board of Directors, its shareholders and other stakeholders.

Corporate Governance exercised in Icelandair Group hf. ensures sound and effective control of the Company´s affairs and a high level of business ethics.

The Board of Directors has prepared a Corporate Governance Statement in compliance with the Icelandic Corporate Governance guidelines which are described in full in the Corporate Governance Statement in the Financial Statements.

It is the opinion of the Board of Directors that Icelandair Group hf. complies with the Icelandic guidelines for Corporate Governance.

Information on matters related to financial risk management is disclosed in note 31.

Statement by the Board of Directors and the CEO
The consolidated financial statements for the year ended 31 December 2014 have been prepared in accordance with International Financial Reporting Standards (IFRSs) as adopted by the EU and additional Icelandic disclosure requirements for consolidated financial statements of listed companies.

According to our best knowledge it is our opinion that the annual consolidated financial statements give a true and fair view of the consolidated financial performance of the Company for the year 2014, its assets, liabilities and consolidated financial position as at 31 December 2014 and its consolidated cash flows for the year 2014.

Further, in our opinion the consolidated financial statements and the endorsement of the Board of Directors and the CEO give a fair view of the development and performance of the Group's operations and its position and describes the principal risks and uncertainties faced by the Group.

The Board of Directors and the CEO have today discussed the consolidated financial statements of Icelandair Group hf. for the year 2014 and confirm them by means of their signatures. The Board of Directors and the CEO recommend that the consolidated financial statements will be approved at the annual general meeting of Icelandair Group hf.

Reykjavík, 5 February 2015.

Board of Directors:

Sigurður Helgason,
Chairman of the Board

Ásthildur Margrét Otharsdóttir

Katrín Olga Jóhannesdóttir

Magnús Magnússon

Úlfar Steindórsson

CEO:

Björgólfur Jóhannsson

Independent Auditors' Report

To the Board of Directors and Shareholders of Icelandair Group hf.

We have audited the accompanying consolidated financial statements of Icelandair Group hf., which comprise the consolidated statement of financial position as at 31 December 2014, the consolidated statements of comprehensive income, changes in equity and cash flows for the year then ended, and notes, comprising a summary of significant accounting policies and other explanatory information.

The Board of Director's and CEO's Responsibility for the Consolidated Financial Statements

The Board of Directors and CEO are responsible for the preparation and fair presentation of these consolidated financial statements in accordance with International Financial Reporting Standards as adopted by the EU, and for such internal control as they determine is necessary to enable the preparation of consolidated financial statements that are free from material misstatement, whether due to fraud or error.

Auditors' Responsibility

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

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

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

Opinion

In our opinion, the consolidated financial statements give a true and fair view of the consolidated financial position of Icelandair Group as at 31 December 2014, and of its consolidated financial performance and its consolidated cash flows for the year then ended in accordance with International Financial Reporting Standards as adopted by the EU.

Report on the Board of Directors report

Pursuant to the legal requirement under Article 104, Paragraph 2 of the Icelandic Financial Statement Act No. 3/2006, we confirm that, to the best of our knowledge, the report of the Board of Directors accompanying the consolidated financial statements includes the information required by the Financial Statement Act if not disclosed elsewhere in the consolidated financial statements.

Reykjavík, 5 February 2015.

KPMG ehf.
Alexander G. Eðvardsson
Auður Þórisdóttir

Consolidated Financial Statements

Consolidated statement of profit or loss and other comprehensive income for the year 2014

	Notes	2014	2013
Continuing operation			
Operating income			
Transport revenue	7	811,002	702,882
Aircraft and aircrew lease		74,754	117,969
Other operating revenue	7	227,541	202,106
		1,113,297	1,022,957
Operating expenses			
Salaries and other personnel expenses	8	273,161	239,432
Aircraft fuel		271,871	242,630
Aircraft and aircrew lease		26,653	34,570
Aircraft maintenance expenses		75,884	81,475
Aircraft handling, landing and communication		82,888	74,316
Other operating expenses	8	228,502	206,824
		958,959	879,247
Operating profit before depreciation and amortisation (EBITDA)		154,338	143,710
Depreciation and amortisation	9	(75,329)	(70,699)
Operating profit (EBIT)		79,009	73,011
Finance income		7,194	6,777
Finance costs		(6,079)	(8,702)
Net finance income (costs)	10	1,115	(1,925)
Share of loss of associates	17	(216)	(38)
Profit before tax		79,908	71,048
Income tax	20	(15,483)	(14,630)
Profit from continuing operations		64,425	56,418
Discontinued operation			
Profit from discontinued operation, net of tax	6	2,074	0
Profit for the year		66,499	56,418
Other comprehensive income			
Items that are or may be reclassified to profit or loss			
Currency translation differences		(5,403)	4,204
Net (loss) profit on hedge of investment, net of tax		(15)	169
Net investment hedge reclassified to profit or loss		719	(111)
Effective portion of changes in fair value of cash flow hedge, net of tax		(23,833)	1,230
Other comprehensive (loss) profit for the year		(28,532)	5,492
Total comprehensive income for the year		37,967	61,910

The notes on pages 75 to 106 are an integral part of these consolidated financial statements.

Amounts are in USD thousand

Consolidated statement of profit or loss and other comprehensive income for the year 2014, continued;

	Notes	2014	2013
Profit attributable to:			
Owners of the Company		66,509	56,386
Non-controlling interests		(10)	32
Profit for the year		66,499	56,418
Total Comprehensive income attributable to:			
Owners of the Company		37,998	61,928
Non-controlling interests		(31)	(18)
Total comprehensive income for the year		37,967	61,910
Earnings per share:			
Basic earnings per share expressed in USD cent per share	26	1.34	1.13
Diluted earnings per share expressed in USD cent per share	26	1.34	1.13
Earnings per share from continuing operations:			
Basic earnings per share (USD)	26	1.30	1.13
Diluted earnings per share (USD)	26	1.30	1.13

The notes on pages 75 to 106 are an integral part of these consolidated financial statements.

Amounts are in USD thousand

Consolidated Statement of Financial Position as at 31 December 2014

	Notes	2014	2013
Assets:			
Operating assets	11-14	319,340	299,197
Intangible assets and goodwill	15-16	175,973	179,676
Investments in associates	17	2,324	2,035
Deferred cost	18	153	258
Receivables and deposits	19	16,413	15,791
Non-current assets		514,203	496,957
Inventories	21	22,906	22,166
Trade and other receivables	22	96,470	114,259
Short term investments	23	30,879	7,955
Cash and cash equivalents	24	184,762	191,538
Current assets		335,017	335,918
Total assets		849,220	832,875
Equity:			
Share capital		40,576	40,576
Share premium		154,705	154,705
Reserves		3,195	31,706
Retained earnings		166,371	118,856
Equity attributable to equity holders of the Company	25	364,846	345,843
Non-controlling interests		208	239
Total equity		365,055	346,082
Liabilities:			
Loans and borrowings	27	49,671	78,489
Payables	28	8,291	23,742
Deferred tax liabilities	20	24,681	27,995
Non-current liabilities		82,643	130,226
Loans and borrowings	27	12,263	43,528
Trade and other payables	29	214,315	159,504
Deferred income	30	174,944	153,535
Current liabilities		401,522	356,567
Total liabilities		484,165	486,793
Total equity and liabilities		849,220	832,875

The notes on pages 75 to 106 are an integral part of these consolidated financial statements.

Amounts are in USD thousand

Consolidated Statement of Changes in Equity for the year 2014

	Attributable to equity holders of the Company						
	Share capital	Share premium	Reserves	Retained earnings	Total	Non-controlling interest	Total equity
2013							
Balance at 1 January 2013 ...	40,576	154,705	26,164	74,230	295,674	257	295,932
Total comprehensive income ..			5,542	56,386	61,928	(18)	61,910
Dividend (0.24 USD cent per share)				(11,760)	(11,760)		(11,760)
Balance at 31 December 2013	40,576	154,705	31,706	118,856	345,842	239	346,082
2014							
Balance at 1 January 2014 ...	40,576	154,705	31,706	118,856	345,842	239	346,082
Total comprehensive income ..			(28,511)	66,509	37,998	(31)	37,967
Dividend (0.38 USD cent per share)				(18,994)	(18,994)		(18,994)
Balance at 31 December 2014	40,576	154,705	3,195	166,371	364,846	208	365,055

Information on changes in other reserves are provided in note 25.

The notes on pages 75 to 106 are an integral part of these consolidated financial statements.

Amounts are in USD thousand

Consolidated Statement of Cash Flows for the year 2014

	Notes	2014	2013
Cash flows from operating activities:			
Profit for the year		66,499	56,418
Adjustments for:			
Depreciation and amortisation	9	75,329	70,699
Other operating items	40	20,979	35,268
Working capital from operations		162,807	162,385
Net change in operating assets and liabilities	41	52,508	68,489
Net cash from operating activities		215,315	230,874
Cash flows to investing activities:			
Acquisition of operating assets	11	(87,893)	(86,916)
Proceeds from the sale of operating assets		1,614	1,594
Acquisition of intangible assets	15	(2,240)	(3,475)
Capitalised deferred cost		(19,160)	(23,849)
Non-current receivables, change		443	(8,622)
Short term investments, change		(22,920)	8,045
Net cash used in investing activities		(130,156)	(113,223)
Cash flows to financing activities:			
Dividend paid	25	(18,994)	(11,760)
Proceeds from non-current borrowings		813	0
Repayment of non-current borrowings		(70,503)	(33,472)
Net cash used in financing activities		(88,684)	(45,232)
(Decrease) increase in cash and cash equivalents		(3,525)	72,419
Effect of exchange rate fluctuations on cash held		(3,251)	2,059
Cash and cash equivalents at beginning of the year		191,538	117,060
Cash and cash equivalents at 31 December	24	184,762	191,538
Investment and financing without cash flow effect:			
Sale of operating assets		0	2,700
Trade and other payables		0	(2,700)
Acquisition of operating assets	11	(10,500)	0
Proceeds from non-current borrowings		10,500	0

Information on interest paid and received are provided in note 42.

The notes on pages 75 to 106 are an integral part of these consolidated financial statements.

Amounts are in USD thousand

Notes

1. Reporting entity

Icelandair Group hf. (the "Company") is a public limited liability company incorporated and domiciled in Iceland. The address of the Company´s registered office is at Reykjavíkurflugvöllur in Reykjavík, Iceland. The consolidated financial statements of the Company as at and for the year ended 31 December 2014 comprise the Company and its subsidiaries, together referred to as the "Group" and individually as "Group entities" and the Group´s interests in associates. The Group is primarily involved in the airline and tourism industry. The Company is listed on the Nasdaq OMX Iceland.

2. Basis of preparation

a. Statement of compliance

The Group's consolidated financial statements have been prepared in accordance with International Financial Reporting Standards (IFRSs) as adopted by the EU. They were authorised for issue by the Company's board of directors on 5 February 2015.

b. Basis of measurement

The consolidated financial statements are prepared on the historical cost basis except that derivative financial instruments and certain short-term investments are stated at their fair values.

Details of the Group's accounting policies, including changes during the year, are included in Note 44.

3. Functional and presentation currency

These Consolidated Financial Statements are presented in U.S dollars (USD), except for information in note 37 about salaries and benefits of management paid for their service to Group companies. Payments to management are denominated and presented in ISK. The Company's functional currency is U.S. dollars (USD). All financial information presented in USD has been rounded to the nearest thousand, unless otherwise indicated.

4. Use of estimates and judgements

In preparing these consolidated financial statements, management has made judgements, estimates and assumptions that affect the application of the Group's accounting policies and the reported amounts of assets, liabilities, income and expenses. Actual results may differ from these estimates.

Estimates and underlying assumptions are reviewed on an ongoing basis. Revisions to estimates are recognised prospectively.

Assumptions and estimation uncertainties

Information about assumptions and estimation uncertainties that have a significant risk of resulting in a material adjustment in the year ending 31 December 2014 is included in the following notes:

Note 16 I measurement of the recoverable amounts of cash-generating units;
Note 18 I deferred cost;
Note 32 I provisions and valuation of financial instruments;
Note 38 I reassessment of taxes.

Measurement of fair values

A number of the Group's accounting policies and disclosures require the measurement of fair value, for both financial and non-financial assets and liabilities.

The Group has an established control framework with respect to the measurement of fair values. The Chief Risk Officer has overall responsibility for overseeing all significant fair value measurements, including Level 3 fair values.

The Risk Committee regularly reviews significant unobservable inputs and valuation adjustments. If third party information, such as broker quotes or pricing services, is used to measure fair values, then management assesses the evidence obtained from the third parties to support the conclusion that such valuations meet the requirements of IFRS, including the level in the fair value hierarchy in which such valuations should be classified.

When measuring the fair value of an asset or a liability, the Group uses market observable data as far as possible. Fair values are categorised into different levels in a fair value hierarchy based on the inputs used in the valuation techniques as follows:

Level 1: quoted prices (unadjusted) in active markets for identical assets or liabilities.
Level 2: inputs other than quoted prices included in Level 1 that are observable for the asset or liability, either directly (i.e. as prices) or indirectly (i.e. derived from prices).
Level 3: inputs for the asset or liability that are not based on observable market data (unobservable inputs).

If the inputs used to measure the fair value of an asset or a liability might be categorised in different levels of the fair value hierarchy, then the fair value measurement is categorised in its entirety in the same level of the fair value hierarchy as the lowest level input that is significant to the entire measurement.

Notes, continued:

4. continued

The Group recognises transfers between levels of the fair value hierarchy at the end of the reporting period during which the change has occurred.

Further information about the assumptions made in measuring fair values is included in the following notes:

Note 23 I short term investments;
Note 30 I deferred income;
Note 32 I derivatives;
Note 32 I non-derivative financial liabilities.

5. Operating segments

Segment information is presented in the consolidated financial statements in respect of the Group's business segments, which are the primary basis of segment reporting. The business segment reporting format reflects the Group's management and internal reporting structure and is divided into two segments; Route network and Tourism services.

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

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

Route network
Seven companies are categorised as being part of the Route Network: Air Iceland, Feria, Fjárvakur - Icelandair Shared Services, Icelandair, Icelandair Cargo, Icelandair Ground Services and Loftleidir Icelandic.

Tourism services
Two companies are categorised as being part of the Tourism Services: Iceland Travel and Icelandair Hotels.

Information on reportable segments

	Route network		Tourism services		Total	
	2014	2013	2014	2013	2014	2013
External revenue	992,159	916,178	121,105	103,777	1,113,264	1,019,955
Inter-segment revenue	131,441	154,661	7,961	5,252	139,402	159,913
Segment revenue	1,123,600	1,070,839	129,066	109,029	1,252,666	1,179,868
Segment EBITDAR*	179,685	176,753	17,990	14,580	197,675	191,333
Operating lease expenses	(28,031)	(36,967)	(11,041)	(9,193)	(39,072)	(46,160)
Segment EBITDA	151,654	139,786	6,949	5,387	158,603	145,173
Finance income	6,277	7,387	835	158	7,112	7,545
Finance costs	(5,556)	(6,741)	(1,076)	(1,125)	(6,632)	(7,866)
Depreciation and amortisation	(72,994)	(67,786)	(2,307)	(1,742)	(75,301)	(69,528)
Share of profit (loss) of equity accounted investees	24	12	(38)	(50)	(14)	(38)
Reportable segment profit before tax	79,405	72,658	4,363	2,628	83,768	75,286
Reportable segment assets	688,272	668,005	30,645	28,411	718,917	696,416
Investment in associates	167	763	457	543	624	1,306
Capital expenditure	113,658	111,611	5,860	2,586	119,518	114,197
Reportable segment liabilities	497,892	479,463	18,783	23,788	516,675	503,251

*EBITDAR means EBITDA before operating lease expenses.

Amounts are in USD thousand

Notes, continued:

5. continued:

Reconciliations of reportable segment revenues, profit or loss, assets and liabilities, and other material items

	2014	2013
Revenue		
Total revenue for reportable segments	1,252,666	1,179,868
Other revenue	33	3,002
Elimination of inter-segment revenue	(139,402)	(159,913)
Consolidated revenue	1,113,297	1,022,957
Profit or loss		
Total profit of reportable segments	83,768	75,286
Unallocated corporate expenses	(3,860)	(4,238)
Consolidated profit before tax	79,908	71,048
Assets		
Total assets for reportable segments	718,917	696,416
Investments in associates	624	1,306
Other assets	129,679	135,153
Consolidated total assets	849,220	832,875
Liabilities		
Total liabilities for reportable segments	516,675	503,251
Elimination of inter-segment liabilities	(32,510)	(16,458)
Consolidated total liabilities	484,165	486,793

Other material items 2014	**Reportable segment totals**	**Adjustments**	**Consolidated totals**
Segment EBITDAR	197,675	(4,265)	193,410
Segment EBITDA	158,603	(4,265)	154,338
Finance income	7,112	82	7,194
Finance costs	(6,632)	553	(6,079)
Depreciation and amortisation	(75,301)	(28)	(75,329)
Share of loss of associates	(14)	(202)	(216)
Capital expenditure	119,518	275	119,793
Other material items 2013			
Segment EBITDAR	191,333	(1,463)	189,870
Segment EBITDA	145,173	(1,463)	143,710
Finance income	7,545	(768)	6,777
Finance costs	(7,866)	(836)	(8,702)
Depreciation and amortisation	(69,528)	(1,171)	(70,699)
Share of loss of associates	(38)	0	(38)
Capital expenditure	114,197	43	114,240

Amounts are in USD thousand

Notes, continued:

6. Discontinued operation

On 30 December 2011 Smartlynx, previously classified as discontinued operations, was sold. Pursuant to the sale Icelandair Group guaranteed aircraft leases on behalf of Smartlynx and had outstanding loans to the Company. Following the sale Icelandair Group made provisions for potential losses due to guarantees and loans. At year-end 2014 all loans had been repaid and all lease guarantees had expired. The provision was therefore reversed resulting in an income of 2.1 million USD net of taxes.

7. Operating income

Transport revenue is specified as follows:	2014	2013
Passengers	766,624	659,992
Cargo and mail	44,378	42,890
Total transport revenue	811,002	702,882

Other operating revenue is specified as follows:

Sale at airports and hotels	77,295	66,358
Revenue from tourism	87,085	73,543
Aircraft and cargo handling services	33,209	32,592
Maintenance revenue	15,766	14,315
Gain on sale of operating assets	204	1,100
Other operating revenue	13,982	14,198
Total other operating revenue	227,541	202,106

8. Operating expenses

Salaries and other personnel expenses are specified as follows:

Salaries	180,424	153,953
Contributions to pension funds	23,152	20,351
Other salary-related expenses	22,453	21,187
Other personnel expenses	47,132	43,941
Total salaries and other personnel expenses	273,161	239,432
Average number of full year equivalents	3,109	2,848

Other operating expenses are specified as follows:

Operating cost of real estates and fixtures	22,418	21,909
Communication	16,577	13,703
Advertising	23,665	20,704
Booking fee and commission	45,464	37,597
Cost of goods sold	23,750	20,926
Customer services	20,510	15,383
Tourism expenses	50,497	44,326
Other operating expenses	25,621	32,276
Total other operating expenses	228,502	206,824

9. Depreciation and amortisation

The depreciation and amortisation charge in profit or loss is specified as follows:

Depreciation of operating assets, see note 11	71,632	67,956
Amortisation of intangible assets, see note 15	3,697	2,743
Depreciation and amortisation recognised in profit or loss	75,329	70,699

Amounts are in USD thousand

Notes, continued:

10. Finance income and finance costs

Finance income and finance costs are specified as follows:

	2014	2013
Interest income on bank deposits	1,319	1,538
Other interest income	900	1,173
Profit from sale of investments	209	0
Net currency exchange gain	4,766	4,066
Finance income total	7,194	6,777
Interest expense on loans and borrowings	5,318	7,860
Other interest expenses	761	842
Finance costs total	6,079	8,702
Net finance income (costs)	1,115	(1,925)

11. Operating assets

Operating assets are specified as follows:

	Aircraft and flight equipment	Buildings	Other property and equipment	Total
Balance at 1 January 2013	375,073	25,510	29,160	429,743
Additions	78,899	1,767	6,250	86,916
Sales and disposals	(48,355)	(198)	(574)	(49,127)
Reclassification to deferred cost	(1,386)	0	0	(1,386)
Reclassification to non-current receivables and deposits	(1,680)	0	0	(1,680)
Effects of movements in exchange rates	279	3,268	3,850	7,397
Balance at 31 December 2013	402,830	30,347	38,686	471,863
Additions	72,030	5,775	20,588	98,393
Sales and disposals	(54,380)	(1,109)	(3,431)	(58,920)
Effects of movements in exchange rates	(204)	(3,294)	(4,903)	(8,401)
Balance at 31 December 2014	420,276	31,719	50,940	502,935
Depreciation and impairment losses				
Balance at 1 January 2013	127,252	6,344	13,150	146,746
Depreciation	62,463	1,455	4,038	67,956
Sales and disposals	(44,648)	(198)	(460)	(45,306)
Effects of movements in exchange rates	123	933	2,214	3,270
Balance at 31 December 2013	145,190	8,534	18,942	172,666
Depreciation	64,674	1,543	5,415	71,632
Sales and disposals	(54,002)	(372)	(3,121)	(57,495)
Effects of movements in exchange rates	(67)	(992)	(2,149)	(3,208)
Balance at 31 December 2014	155,795	8,713	19,087	183,595
Carrying amounts				
At 1 January 2013	247,821	19,166	16,010	282,997
At 31 December 2013	257,640	21,813	19,744	299,197
At 31 December 2014	264,481	23,006	31,853	319,340
Depreciation ratios	6-33%	2-6%	5-33%	

Acquisition of operating assets 2014 includes two Boeing 757 aircraft and engine overhauls amounting to USD 50.1 million.

Amounts are in USD thousand

Notes, continued:

12. Mortgages and commitments

The Group's operating assets, aircraft and spare parts are mortgaged to secure debt. The remaining balance of the debt amounted to USD 49.8 million at year end 2014 (2013: USD 107.6 million). The Group owns 29 aircraft, of which 22 are unencumbered, including 14 Boeing 757.

13. Insurance value of aircraft and flight equipment

The insurance value and carrying amount of the Group's aircraft and related equipment at year-end is specified as follows:

	Insurance value		Carrying amount	
	2014	2013	2014	2013
Boeing - 21 / 19 aircraft	577,000	527,000	218,780	213,512
Other aircraft	41,075	42,608	20,619	22,441
Flight equipment	64,642	71,816	25,082	21,687
Total aircraft and flight equipment	682,717	641,424	264,481	257,640

14. Insurance value of buildings and other operating assets

The principal buildings owned by the Group are the following:

	Official assessment value		Insurance value		Carrying amount	
	2014	2013	2014	2013	2014	2013
Maintenance hangar, Keflavík	15,241	15,263	29,517	32,061	4,167	4,960
Freight building, Keflavík	3,439	3,683	7,198	7,267	1,115	2,489
Office building, Reykjavík	5,377	7,875	10,904	11,949	6,651	7,722
Service building, Keflavík	3,834	4,079	7,198	7,830	3,471	1,261
Other buildings in Reykjavik	6,112	6,504	9,475	10,343	1,598	2,001
Other buildings	2,892	3,742	8,183	10,604	6,004	3,380
Buildings total	36,895	41,146	72,475	80,054	23,006	21,813

Official valuation of the Group's leased land for buildings at 31 December 2014 amounted to USD 10.4 million (2013: USD 7.9 million) and is not included in the statement of financial position.

The insurance value of the Group's other operating assets and equipment amounted to USD 75,0 million at year end 2014 (2013: USD 50.9 million). The carrying amount at the same time was USD 31.9 million (2013: USD 19.7 million).

Amounts are in USD thousand

Notes, continued:

15. Intangible assets and goodwill

Intangible assets and goodwill are specified as follows:

	Goodwill	Trademarks and slots	Customer relations	Other intangibles	Total
Cost					
Balance at 1 January 2013	148,514	35,958	5,154	6,213	195,839
Additions	0	0	0	3,475	3,475
Sales and disposals	0	0	0	(416)	(416)
Effect of movements in exchange rates	2,132	27	48	98	2,305
Balance at 31 December 2013	150,646	35,985	5,202	9,370	201,203
Additions	0	0	0	2,240	2,240
Sales and disposals	0	0	0	(1,833)	(1,833)
Effect of movements in exchange rates	(2,130)	(24)	(44)	(182)	(2,380)
Balance at 31 December 2014	148,516	35,961	5,158	9,595	199,230
Amortisation and impairment losses					
Balance at 1 January 2013	11,431	2,605	4,102	986	19,124
Amortisation	0	0	342	2,401	2,743
Sales and disposals	0	0	0	(416)	(416)
Effect of movements in exchange rates	0	0	36	40	76
Balance at 31 December 2013	11,431	2,605	4,480	3,011	21,527
Amortisation	0	0	360	3,337	3,697
Sales and disposals	0	0	0	(1,833)	(1,833)
Effect of movements in exchange rates	0	0	(39)	(95)	(134)
Balance at 31 December 2014	11,431	2,605	4,801	4,420	23,257
Carrying amounts					
At 1 January 2013	137,083	33,353	1,052	5,227	176,715
At 31 December 2013	139,215	33,380	722	6,359	179,676
At 31 December 2014	137,085	33,356	357	5,175	175,973

16. Impairment test

Goodwill and other intangible assets that have indefinite life are tested for impairment at each reporting date. These assets were recognised at fair value on acquistion dates. Goodwill and other intangible assets with indefinite life are specified as follows:

	2014	2013
Goodwill	137,085	139,215
Trademarks and airport slots	33,356	33,380
Total	170,441	172,595

The decrease in the carrying amount of goodwill is due to translation differences of subsidiaries with functional currencies other than USD.

For the purpose of impairment testing, goodwill is allocated to the subsidiaries which represent the level within the Group at which the goodwill is monitored for internal management purposes. The aggregate carrying amounts of goodwill allocated to each cash generated unit (CGU) are as follows:

	Goodwill		Trademarks and slots	
	2014	2013	2014	2013
Route network	134,933	136,778	33,356	33,380
Tourism services	2,152	2,437	0	0
Total goodwill	137,085	139,215	33,356	33,380

The recoverable amounts of cash-generating units was based on their value in use and were determined by discounting the future cash flows generated from the continuing use of the CGU. Cash flows were projected based on actual operating results and a 5 - 10 year business plan. Cash flows were extrapolated for determining the residual value using a constant nominal growth rate which was consistent with the long-term average growth rate for the industry. Management believes that this forecast period was justified due to the long-term nature of the business.

Amounts are in USD thousand

Notes, continued:

16. continued:

The values assigned to the key assumptions represent management's assessment of future trends in the airline, transportation and the tourism industry and are based on both external and internal sources (historical data). Value in use was based on the following key assumptions:

	Route network		Tourism services	
	2014	2013	2014	2013
Long term growth rate	2,5-4,0%	2,5-4,0%	2,5-4%	4.0%
Revenue growth:				
Weighted average 2014 / 2013	5.8%	6.4%	6.4%	19.9%
2015 - 2025 / 2014 - 2024	6.9%	8.1%	8.1%	11.9%
Budgeted EBITDA growth	8.9%	5.4%	5.4%	10.4%
WACC	8,3-13,6%	10,0-14,8%	10,0-14,8%	12.4%
Debt leverage	10,2-56,1%	18,0-56,5%	18,0-56,5%	23.5%
Interest rate for debt	5,5-7,7%	7,7-9,4%	7,7-9,4%	6.7%
Recoverable amounts	551,909	775,398	32,656	39,307

Changes in key assumptions would have the following impact on the carrying amount of goodwill:

	2014	2013
Long term growth rate - 1%	(23,505)	0
WACC +1%	(28,784)	0
EBITDA - 5%	(55,111)	0

No impairment loss is recognised in the Financial Statements

17. Investment in associates

The Group has interests in a number of individually immaterial associates. The carrying amount and share of loss of the associates is as follows:

	2014	2013
Carrying amount of interests in associates	2,324	2,035
Share of loss from operation	(216)	(38)

18. Deferred cost

Deferred cost consists of prepaid lease on housing and amounts paid for engine overhauls and heavy maintenance of leased aircraft which will be expensed over the lease period of the aircraft. Deferred cost is specified as follows:

Deferred cost	237	1,025
Current portion, classified as prepayments among receivables	(84)	(767)
Total deferred cost	153	258

Deferred cost will be expensed as follows:

Expensed in 2014	-	767
Expensed in 2015	84	89
Expensed in 2016	47	52
Expensed in 2017	51	56
Expensed in 2018	55	61
Total deferred cost, including current maturities	237	1,025

Amounts are in USD thousand

Notes, continued:

19. Non-current receivables and deposits

Non-current receivables consist of notes, deposits for aircraft and engine lease agreements and various other travel related security fees.

	2014	2013
Non-current receivables and deposits are specified as follows:		
Loans, effective interest rate 6%	300	466
Deposits	10,268	13,510
Prepayments on aircraft purchases	11,550	9,612
	22,118	23,588
Current maturities	(5,705)	(7,797)
Non-current receivables and deposits total	16,413	15,791

Contractual repayments are specified as follows:

	2014	2013
Repayments in 2014	-	7,797
Repayments in 2015	5,705	2,156
Repayments in 2016	511	99
Repayments in 2017	586	934
Repayments in 2018	4,897	9,627
Repayments in 2019	4,441	418
Subsequent	5,978	2,557
Total non-current receivables and deposits, including current maturities	22,118	23,588

Non-current receivables and deposits denominated in currencies other than the functional currency comprise USD 0.9 million (2013: USD 1.3 million).

20. Taxes

Tax recognised in profit or loss	**2014**	**2013**
Current tax expense		
Current year	12,362	6,613
	12,362	6,613
Deferred tax expense		
Origination and reversal of temporary differences	3,084	8,256
Exchange rate difference	556	(239)
	3,640	8,017
Total tax expense recognised in profit or loss	16,002	14,630
Tax expense from continuing operations	15,483	14,630
Tax expense from discontinued operations	519	0
	16,002	14,630

Tax recognised in other comprehensive income

	2014	2013
Net profit on hedge of net investment in foreign operations	0	(68)
Effective portion of changes in fair value of cash flow hedge	5,940	0
Exchange rate difference	458	0
Total tax recognised in other comprehensive income	6,398	(68)

Reconciliation of effective tax rate

		2014		2013
Profit before tax from continuing operations		79,908		71,048
Income tax according to current tax rate	20.0%	15,982	20.0%	14,210
Tax exempt revenue	0.0%	0	(0.0%)	(27)
Non-deductible expenses	0.2%	190	0.2%	175
Other items	(0.2%)	(170)	0.4%	272
Effective tax rate	20.0%	16,002	20.6%	14,630

Amounts are in USD thousand

Notes, continued:

20. continued:

Recognised deferred tax liabilities

Deferred tax liabilities are specified as follows:

	2014	2013
Deferred tax liabilities 1 January	27,995	19,671
Exchange rate difference	(1,014)	239
Income tax recognised in profit or loss	16,002	14,630
Income tax recognised in other comprehensive income	(5,940)	68
Income tax payable	(12,362)	(6,613)
Deferred tax liabilities 31 December	24,681	27,995

Deferred tax liabilities are attributable to the following:

	Assets		Liabilities		Net	
	2014	2013	2014	2013	2014	2013
Operating assets	0	0	(29,810)	(26,173)	(29,810)	(26,173)
Intangible assets	0	0	(1,217)	(2,206)	(1,217)	(2,206)
Derivatives	5,991	60	0	0	5,991	60
Trade receivables	199	661	0	0	199	661
	6,190	721	(31,027)	(28,379)	(24,837)	(27,658)
Tax loss carry-forwards	557	0	0	0	557	0
Other items	0	0	(401)	(337)	(401)	(337)
Deferred income tax	6,747	721	(31,428)	(28,716)	(24,681)	(27,995)

Movements in deferred tax balance during the year

	1 January	Recognised in profit or loss	Exchange rate difference	Recognised in other compre-hensive income and equity	31 December
2014					
Operating assets	(26,173)	(4,273)	636	0	(29,810)
Intangible assets	(2,206)	908	81	0	(1,217)
Derivatives	60	0	(9)	5,940	5,991
Trade receivables	661	(464)	2	0	199
Tax loss carry-forwards	0	580	(23)	0	557
Other items	(337)	(391)	327	0	(401)
	(27,995)	(3,640)	1,014	5,940	(24,681)
2013					
Operating assets	(22,732)	(3,923)	482	0	(26,173)
Intangible assets	(2,007)	(336)	137	0	(2,206)
Derivatives	90	0	(2)	(28)	60
Trade receivables	601	53	7	0	661
Tax loss carry-forwards	4,967	(4,062)	(905)	0	0
Other items	(590)	251	42	(40)	(337)
	(19,671)	(8,017)	(239)	(68)	(27,995)

The tax calculations above do not take into consideration the effects of reassessment of taxes for the years 2007 to 2011 that took place in December 2013. The management does not agree with the ruling and an appeal to the State Internal Revenue Board has been filed. If the reassessment will however be confirmed the Company's net equity will be reduced by approximately USD 11 million. Further information on the reassessment is provided in note 38.

Amounts are in USD thousand

Notes, continued:

21. Inventories

Inventories are specified as follows:

	2014	2013
Spare parts	18,377	17,500
Other inventories	4,529	4,666
Inventories total	22,906	22,166

22. Trade and other receivables

Trade and other receivables are specified as follows:

	2014	2013
Trade receivables	60,532	76,537
Prepayments	3,662	3,905
Restricted cash	12,407	8,686
Derivatives used for hedging	2,016	1,853
Current maturities of long term-receivables	5,705	7,797
Other receivables	12,148	15,481
Trade and other receivables total	96,470	114,259

At year end trade receivables are presented net of an allowance for doubtful debts of USD 5.4 million (2013: USD 11.9 million).

Prepaid expenses which relate to subsequent periods amounted to USD 3.7 million (2013: USD 3.9 million) at year end. The prepayments consist mainly of insurance premiums, software licenses and prepaid leases.

Restricted cash is held in bank accounts pledged against credit card, derivative and tourism guarantees.

The Group's exposure to credit and currency risks and impairment losses related to trade and other receivables is disclosed in note 31.

23. Short term investments

Short term investments at year end consist of securities listed on stock exchanges in Luxemburg and Iceland and fixed deposits. They are accounted at fair value at year end, based on market value.

24. Cash and cash equivalents

Cash and cash equivalents are specified as follows:

	2014	2013
Securities	1,574	4,956
Bank deposits	182,866	186,192
Cash on hand	322	390
Cash and cash equivalents total	184,762	191,538

25. Equity

(i) Share capital

The Company's share capital amounts to ISK 5.0 billion according to its Articles of Association. Shareholders are entitled to receive dividends as declared from time to time and are entitled to one vote per share of one ISK.

The Company held treasury shares in the amount of ISK 25 million at year end 2014 (2013: ISK 25 million).

(ii) Share premium

Share premium represents excess of payment above nominal value (ISK 1 per share) that shareholders have paid for shares sold by the Company. According to Icelandic Companies Act, 25% of the nominal value of share capital must be held in reserve. The balance of the share premium account can be used to offset losses not covered by other reserves or to offset stock splits.

(iii) Other reserves

The hedging reserve comprises the effective portion of the cumulative net change in the fair value of cash flow hedging instruments related to hedged transactions that have not yet occurred.

The translation reserve comprises all currency differences arising from the translation of the financial statements of subsidiaries having functional currencies other than the Group, as well as from the translation of liabilities that hedge net investment.

Amounts are in USD thousand

Notes, continued:

25. continued:

Other reserves are specified as follows:

	Hedging reserve	Translation reserve	Total reserves
Balance 1 January 2013	(1,338)	27,502	26,164
Currency translation differences		4,254	4,254
Currency translation differences reclassified to profit or loss		169	169
Net loss on hedge of investment, net of tax		(111)	(111)
Effective portion of changes in fair value of cash flow hedges, net of tax	1,230		1,230
Balance at 31 December 2013	(108)	31,814	31,706
Currency translation differences		(5,382)	(5,382)
Net profit on hedge of investment, net of tax		(15)	(15)
Net investment hedge reclassified to profit or loss		719	719
Effective portion of changes in far value of cash flow hedges, net of tax	(23,833)		(23,833)
Balance at 31 December 2014	(23,941)	27,136	3,195

(iv) Dividends

The Board of Directors has approved to the following dividend policy: "The Company's goal is to declare 20-40% of annual net profit as dividend. Final decision on dividend payments will be based on the financial position of the Company, operating capital requirements and market conditions."

Dividend amounting to USD 19.0 million was paid to shareholders in the year 2014 (2013: USD 11.8 million).

The Board of Directors proposes a dividend payment to shareholders in 2015 of ISK 2.500 million, equal to USD 19.6 million, which represents 30% of profit for the year 2014.

26. Earnings per share

Basic earnings per share is calculated by dividing the net profit attributable to equity holders of the Parent by the weighted average number of outstanding shares during the year. The calculation of diluted earnings per share is identical to basic earnings per share as no convertible notes or stock options have been issued.

	2014	2013
Basic earnings per share:		
Profit for the year attributable to equity holders of the parent company	66,509	56,386
Weighted average number of shares for the year	4,974,540	4,974,540
Basic earnings per share of ISK 1 expressed in USD cent per share	1.34	1.13
Diluted earnings per share expressed in USD cent per share	1.34	1.13
Earnings per share from continuing operations:		
Profit from continuing operations attributable to equity holders of parent company	64,435	56,386
Basic earnings per share (USD)	1.30	1.13
Diluted earnings per share (USD)	1.30	1.13

27. Loans and borrowings

This note provides information on the contractual terms of the Group´s interest-bearing loans and borrowings, which are measured at amortised cost. For more information about the Group´s exposure to interest rate, foreign currency and liquidity risk, see note 31.

Loans and borrowings are specified as follows:

Secured bank loans	49,755	107,621
Unsecured loans	12,179	14,396
Total loans and borrowings	61,934	122,017
Current maturities	(12,263)	(43,528)
Total non-current loans and borrowings	49,671	78,489

Amounts are in USD thousand

Notes, continued:

27. continued:

Terms and debt repayment schedule:

	Currency	Nominal interest rates year end 2014	Year of maturity	Total remaining balance 2014	2013
Secured bank loans	USD	5.5%	2017-2023	47,974	74,921
Secured bank loans	EUR			0	15,518
Secured bank loans	ISK	7.2%	2023	968	16,209
Secured bank loans, indexed	ISK	6.3%	2021-2028	813	973
Unsecured bond issue, indexed	ISK	5.7%	2023	12,179	14,396
Total interest bearing liabilities				61,934	122,017

Repayments of loans and borrowings are specified as follows:	2014	2013
Repayments in 2014	-	43,528
Repayments in 2015	12,263	15,898
Repayments in 2016	12,684	16,350
Repayments in 2017	12,755	29,471
Repayments in 2018	8,125	7,430
Repayments in 2019	2,388	1,604
Subsequent repayments	13,719	7,736
Total loans and borrowings	61,934	122,017

On December 19th the Company sold bonds to Icelandic investors for the amount of USD 23,7 million. The bonds were paid in the beginning of January 2015 and are therefore not accounted for in the Balance Sheet at year end. The bonds are denominated in USD and carry 4,25% fixed interest paid semi-annually and have a maturity date in January 2020.

28. Non-current payables

Non-current payables correspond to accrued engine overhaul cost of leased aircraft and security deposits from lease contracts to be realized after 2015. Non-current obligations are specified as follows:

	2014	2013
Non-current payables	39,412	43,907
Current portion, classified in trade and other payables	(31,121)	(20,165)
Total non-current payables	8,291	23,742

Non-current payables will be repaid as follows:		
Repayments in 2014	-	20,165
Repayments in 2015	31,121	19,417
Repayments in 2016	2,212	900
Repayments in 2017	1,123	0
Repayments in 2018	2,481	1,750
Repayments in 2019	800	0
Subsequent repayments	1,675	1,675
Total non-current payables, including current maturities	39,412	43,907

29. Trade and other payables

Trade and other payables are specified as follows:

Trade payables	40,983	38,125
Current portion of engine overhaul and security deposits from lease contracts	31,121	20,165
Derivatives used for hedging	31,925	2,050
Income tax payable	12,362	6,613
Other payables	97,924	92,551
Total trade and other payables	214,315	159,504

The Group's exposure to currency and liquidity risk related to trade and other payables is disclosed in note 31.

Amounts are in USD thousand

Notes, continued:

30. Deferred income

Sold unused tickets, fair value of unutilized frequent flyer points and other prepayments are presented as deferred income in the statement of financial position.

Deferred income is specified as follows:	2014	2013
Sold unused tickets	148,346	129,373
Frequent flyer points	13,400	12,610
Other prepayments	13,198	11,552
Total deferred income	174,944	153,535

The amount allocated to frequent flyers points is estimated by reference to the fair value of the discounted services for which they could be redeemed, since the fair value of the points themselves is not directly observable. The fair value of the discounted services for which the points, granted through a customer loyalty programme, can be redeemed takes into account the expected redemption rate and the timing of such expected redemptions. That amount is recognised as deferred income.

31. Financial risk management

Overview

The Group has exposure to the following financial risks:
- credit risk
- liquidity risk
- market risk

This note presents information about the Group's exposure to each of the above risks, the Group's objectives, policies, and processes for measuring and managing risk, and the Group's management of capital. Further quantitative disclosures are included throughout these consolidated financial statements.

Risk management framework

The Board of Directors has overall responsibility for the establishment and oversight of the Group's risk management framework. The Board has established the Risk Management Committee, which is responsible for developing and monitoring the Group's risk management policies. The committee reports regularly to the Board of Directors on its activities.

The Group's risk management policies are established to identify and analyse the risks faced by the Group, to set appropriate risk limits and controls, and to monitor risks and adherence to limits. Risk management policies and systems are reviewed regularly to reflect changes in market conditions and the Group's activities. The Group, through its training and management standards and procedures, aims to develop a disciplined and constructive control environment in which all employees understand their roles and obligations.

The Group Audit Committee oversees how management monitors compliance with the Group's risk management policies and procedures, and reviews the adequacy of the risk management framework in relation to the risks faced by the Group. The Group Audit Committee is assisted in its oversight role by Internal Audit which undertakes both regular and ad hoc reviews of risk management controls and procedures, the results of which are reported to the Audit Committee.

Credit risk

Credit risk is the risk of financial loss to the Group if a customer or counterparty to a financial instrument fails to meet its contractual obligations, and arises principally from the Group's receivables from customers.

Exposure to credit risk

The carrying amounts of financial assets represents the maximum credit exposure. The maximum exposure to credit risk at the reporting date was as follows:

		Carrying amount	
	Note	2014	2013
Non-current receivables and deposits	19	16,413	15,791
Trade and other receivables	22	92,808	110,354
Short term investments	23	30,879	7,955
Cash and cash equivalents	24	184,762	191,538
		324,862	325,638

Amounts are in USD thousand

Notes, continued:

31. continued:

Trade and other receivables

The Group's exposure to credit risk is influenced mainly by the individual characteristics of each customer.

Credit risk is linked to trade receivables, investment in liquid assets and agreements with financial institutions related to financial operations, e.g. hedging. The relative spread of trade receivables across counterparties is also crucial for credit risk exposure. The risk involved is directly related to the fulfilment of outstanding obligations of the Group's counterparties. The Group is aware of potential losses related to credit risk exposure and chooses its counterparties subject to business experience and satisfactory credit ratings.

The Group establishes an allowance for impairment that represents its estimate of incurred losses in respect of trade and other receivables. The main components of this allowance are a specific loss component that relates to individually significant exposures, and a collective loss component established for groups of similar assets in respect of losses that have been incurred but not yet identified. The collective loss allowance is determined based on historical data of payment statistics for similar financial assets.

Guarantees
The Group's policy is to provide financial guarantees only to wholly-owned subsidiaries. However at year end 2014 the Group is still guaranteeing from divested companies (see note 38), the PDP payments of one 787 Boeing Dreamliner order but the economical proceeds from these orders have been sold to the creditors in relation to the Group's financial restructuring in the year 2010.

Impairment losses
The aging of trade receivables at the reporting date was as follows:

	Gross 2014	Allowance for Impairment 2014	Gross 2013	Allowance for Impairment 2013
Not past due	54,876	(315)	52,815	(569)
Past due 0-30 days	2,830	(117)	5,861	(523)
Past due 31-120 days	3,081	(457)	6,578	(462)
Past due 121-365 days	615	(409)	19,422	(7,602)
More than one year	4,520	(4,092)	3,770	(2,753)
Total	65,922	(5,390)	88,446	(11,909)

Movements in the allowance for impairment in respect of trade receivables during the year were as follows:

	2014	2013
Balance at 1 January	11,909	8,668
Impairment loss allowance, (decrease) increase	(1,766)	3,701
Amounts written off	(4,684)	(508)
Exchange rate difference	(69)	48
Balance at 31 December	5,390	11,909

Based on historical default rates, the management believes that minimal impairment allowance is necessary in respect of trade receivables not past due or past due by 30 days; a significant part of the balance relates to customers that have a good track record with the Group.

The allowance account in respect of trade receivables is used to record impairment losses unless the Group is satisfied that no recovery of the amount owing is possible; at that point the amount is considered irrecoverable and is written off against the financial asset directly.

Amounts are in USD thousand

Notes, continued:

31. continued:

Liquidity risk

Liquidity risk is the risk that the Group will encounter difficulty in meeting the obligations associated with its financial liabilities that are settled by delivering cash or another financial asset. The Group's approach to managing liquidity is to ensure, as far as possible, that it will always have sufficient liquidity to meet its liabilities when due, under both normal and stressed conditions, without incurring unacceptable losses or risking damage to the Group's reputation.

The Group policy is to divide liquid assets into three classes depending on duration and match them against the Group's liquidity preferences laid out by the management on annual basis. Classes one and two include the estimated minimum of accessible funds for operational liquidity, but differ in terms of asset types and duration. Class three includes assets of longer duration for strategic liquidity, such as medium term investments. The amounts in each class of assets are targeted once a year with reference to a number of economic indicators, most importantly, the estimated level of three month operational costs, but also w.r.t. the estimated annual level of fixed costs and turnover.

Following are the contractual maturities of financial liabilities, including estimated interest payments:

31 December 2014	Carrying amount	Contractual cash flows	Within 12 months	1–2 years	2–5 years	More than 5 years
Financial liabilities						
Unsecured bank loans	12,179	15,906	1,767	1,767	5,302	7,070
Secured loans	49,755	61,675	14,576	14,928	23,423	8,748
Payables & prepayments	222,606	222,606	214,145	2,381	4,405	1,675
Exposure to liquidity risk	284,540	300,187	230,488	19,076	33,130	17,493
31 December 2013						
Financial liabilities						
Unsecured bond issue	14,396	19,282	1,928	1,928	5,785	9,641
Secured loans	107,621	124,844	47,683	19,689	56,082	1,390
Payables & prepayments	183,246	183,246	159,504	19,417	2,650	1,675
Exposure to liquidity risk	305,263	327,372	209,115	41,034	64,517	12,706

Unused loan commitments at year end 2014 amounted to USD 3.9 million (2013: USD 4.3 million).

In addition to the liquidity exposure presented in the balance sheet the Group is exposed to off balance sheet liabilities. Further information on these liabilities are provided in note 33 and 36.

Market risk

Market risk emerges from changes in market prices, such as foreign exchange rates, interest rates, carbon prices and fuel prices, as those changes will affect the Group's income or the value of its holdings of financial instruments. The objective of market risk management is to manage and control market risk exposures within acceptable parameters, while optimising the return.

The Group uses spot and forward trading, swaps and derivatives in order to manage market risks. All such transactions are carried out within the guidelines set by the Board of Directors. The Group seeks to apply hedge accounting in order to manage volatility in profit or loss.

Amounts are in USD thousand

Notes, continued:

31. continued:

Currency risk
The Group is exposed to currency risk on sales, purchases and borrowings that are denominated in a currency other than the respective functional currencies of Group entities.

The Group seeks to reduce its foreign exchange exposure arising from currency mismatch in the cashflow by netting receipts and payments in each individual currency and by internal trading within the Group. The residual net currency exposures of the Group which need to be met by external sources are short positions in ISK and USD which are financed by a surplus of European currencies, most importantly EUR and Scandinavian currencies but also GBP and CAD. The exposure is hedged 40-80% 9-12 months forward with spot and forward contracts.

Exposure to currency risk
The Group's exposure to currency risk in its major currencies is as follows:

2014	**ISK**	**EUR**	**GBP**	**DKK**	**SEK**	**CAD**
Net balance sheet exposure	(19,996)	1,310	(11,963)	(296)	(960)	7,438
Next 12 months forecast sales	326,050	263,390	75,216	40,281	37,009	65,015
Next 12 months forecast purchase	(443,990)	(161,437)	(45,781)	(17,727)	(3,806)	(15,705)
Net forecast transaction contracts	(137,936)	103,263	17,472	22,258	32,243	56,748
Forward exchange contracts	42,416	(46,800)	(4,622)	0	0	(12,584)
Net currency exposure	(95,519)	56,463	12,850	22,258	32,243	44,164

2013	**ISK**	**EUR**	**GBP**	**DKK**	**SEK**	**NOK**
Net balance sheet exposure	(25,872)	(18,759)	(7,072)	919	2,715	1,911
Next 12 months forecast sales	339,060	237,680	73,705	39,890	47,195	43,760
Next 12 months forecast purchase	(409,650)	(167,882)	(40,722)	(14,670)	(4,141)	(4,799)
Net forecast transaction contracts	(96,462)	51,039	25,911	26,139	45,769	40,872
Forward exchange contracts	0	(64,711)	0	0	0	0
Net currency exposure	(96,462)	(13,672)	25,911	26,139	45,769	40,872

The following significant exchange rates of USD applied during the year:

	Average rate		**Year-end spot rate**	
	2014	**2013**	**2014**	**2013**
ISK	0.0085	0.0082	0.0079	0.0087
EUR	1.33	1.33	1.22	1.38
GBP	1.65	1.56	1.56	1.65
CAD	0.91	0.97	0.86	0.94
DKK	0.18	0.18	0.16	0.18
SEK	0.15	0.15	0.13	0.16
NOK	0.16	0.17	0.13	0.16

Amounts are in USD thousand

Notes, continued:

31. continued:

Sensitivity analysis

A 10% strengthening of the USD against the following currencies at 31 December would have increased (decreased) post-tax equity and profit or loss by the amounts shown below. This analysis assumes that all other variables, in particular interest rates, remain constant. This analysis is performed on the same basis as for 2013.

	Equity	Profit or loss
2014		
ISK	7,642	7,642
EUR	(4,517)	(4,517)
GBP	(1,028)	(1,028)
DKK	(1,781)	(1,781)
SEK	2,579	2,579
CAD	3,533	3,533
2013		
ISK	7,717	7,717
EUR	1,094	864
GBP	(2,073)	(2,073)
DKK	(2,091)	(2,091)
SEK	(3,662)	(3,662)
NOK	(3,270)	(3,270)

A 10% weakening of the USD against the above currencies would have had the equal but opposite effect on the above currencies to the amounts shown above, on the basis that all other variables remain constant.

Interest rate risk

The fair value of a fixed rate instrument will fluctuate because of changes in market interest rates. The cash flow of variable rate instruments will also fluctuate with changes in market interest rates. The Group follows a policy of hedging 40-80% of the net interest rate cash flow exposure of long-term financing with up to a 5-year horizon. This is achieved by using fixed rate loan and fixed for floating swap contracts, which carrying amount is evaluated at fair value.

At the reporting date the interest rate profile of the Group´s interest bearing financial instruments was as follows:

	Carrying amount	
	2014	2013
Fixed rate instruments		
Financial assets	2,864	3,000
Financial liabilities	0	0
	2,864	3,000
Effect of derivatives	(32,595)	84
	(29,731)	3,084
Variable rate instruments		
Financial assets	182,866	186,192
Financial liabilities	(36,264)	(79,811)
	146,602	106,381

Amounts are in USD thousand

Notes, continued:

31. continued:

Fair value sensitivity analysis for fixed rate instruments
The Group does not account for any fixed rate financial assets and liabilities at fair value through profit or loss. The Group does designate derivatives for the purpose of fuel, carbon, fx and interest rate hedging as hedging instruments under a fair value hedge accounting model. Interest rate changes affect the fixed rate instruments carrying amount through equity.

A change of 100 basis points in interest rates at the reporting date would have increased (decreased) equity and profit or loss by the amounts stated below. This analysis assumes that all other variables, in particular foreign currency rates, remain constant.

	100 bp increase	100 bp decrease
31 December 2014		
Fixed rate instruments	(26)	26
Effects of derivatives	425	(164)
Fair value sensitivity (net)	399	(138)
31 December 2013		
Fixed rate instruments	205	(112)
Fair value sensitivity (net)	205	(112)

Cash flow sensitivity analysis for variable rate instruments
A change of 100 basis points in interest rates at the reporting date would have increased (decreased) equity and profit or loss by the amounts stated below. This analysis assumes that all other variables, in particular foreign currency rates, remain constant.

	100 bp increase	100 bp decrease
31 December 2014		
Variable rate instruments	1,466	(1,466)
Cash flow sensitivity (net)	1,466	(1,466)
31 December 2013		
Variable rate instruments	1,064	(1,064)
Cash flow sensitivity (net)	1,064	(1,064)

Other market price risk
Fuel price risk
The Group maintains a policy of hedging fuel price exposure by a ratio from 40% and up to 60%, from a minimum of 9 months forward to a maximum of 12 months.

Sensitivity analysis
The following table demonstrates the sensitivity of the financial instruments in place at year end to a reasonably possible change in fuel prices, with all other variables held constant, on profit before tax and equity:

	Effect on equity		Effect on profit before tax	
	2014	2013	2014	2013
Increase in fuel prices by 10%	10,980	6,800	0	0
Decrease in fuel prices by 10%	(10,980)	(6,800)	0	0

Capital management
The Board's policy is to maintain a strong capital base for the benefit of investor, creditor and market confidence and to sustain future development of the business. The policy is to hold in reserve the equivalent of three months operating cost of which 30% of the benchmark can be in the form of unused lines of credit. Furthermore according to the policy the equity ratio shall be no less than 35%.

Amounts are in USD thousand

Notes, continued:

32. Financial instruments and fair values

The following table shows the carrying amounts and fair values of financial assets and financial liabilities. It does not include fair value information for financial assets and financial liabilities not measured at fair value if the carrying amount is a reasonable approximation of fair value.

	Carrying amount 2014	Fair value 2014	Carrying amount 2013	Fair value 2013
Derivatives, included in loans and receivables	2,016	2,016	1,853	1,853
Short term investments	30,879	30,879	7,955	7,955
Unsecured bond issue	(12,179)	(12,479)	(14,396)	(17,398)
Secured loans	(49,755)	(52,092)	(107,621)	(117,219)
Derivatives, included in payables and prepayments	(31,925)	(31,925)	(2,050)	(2,050)
Total	(60,964)	(63,601)	(114,259)	(126,859)

Fair value hierarchy:

The table below analyses the fair value of assets and liabilities and their levels in the fair value hierarchy:

31 December 2014	Level 1	Level 2	Level 3	Total
Derivatives, included in loans and receivables		2,016		2,016
Short term investments	30,879			30,879
Unsecured bond issue			(12,479)	(12,479)
Secured loans			(52,092)	(52,092)
Derivatives, included in payables and prepayments		(31,925)		(31,925)
Total	30,879	(29,909)	(64,571)	(63,601)
31 December 2013				
Derivatives, included in loans and receivables		1,853		1,853
Short term investments	7,955			7,955
Unsecured bond issue			(17,398)	(17,398)
Secured loans			(117,219)	(117,219)
Derivatives, included in payables and prepayments		(2,050)		(2,050)
Total	7,955	(197)	(134,617)	(126,859)

The basis for determining the levels is disclosed in note 4.

Non-derivative financial liabilities

Fair value, which is determined for disclosure purposes, is calculated based on the present value of future principal and interest cash flows, discounted at market rate of interest at the reporting date. In respect of the liability component of convertible notes, the market rate of interest is determined by reference to similar liabilities that do not have a conversion option.

Derivatives

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

The fair value of interest rate swaps is based on broker quotes. If not available the fair value is based on the discounted cashflow difference of the contractual fixed interest payment and the floating interest receivable.

Fair values reflect the credit risk of the instrument and include adjustments to take account of the credit risk of the Group entity and counterparty when appropriate.

Amounts are in USD thousand

Notes, continued:

33. Off-balance sheet items

Leases as lessee

As a lessee the Group has in place operating leases for 9 aircraft at the end of December 2014. The leases are for 4 Boeing 757 aircraft, 2 Boeing 767 aircraft and 3 Boeing 737 aircraft. The lease agreements last from 9 months to 6,5 years. The Group also has in place operating leases for storage facilities, hotels, equipment and fixtures for its operations, the longest until the year 2039. During the year USD 39.1 million was recognised as an expense in profit or loss in respect of operating leases (2013: USD 46.2 million). At year end 2014 the leases are payable as follows in nominal amounts for each year:

	Real estate	Aircraft	Other	Total 2014	Total 2013
In the year 2014	-	-	-	-	40,908
In the year 2015	12,773	22,293	4,569	39,635	36,858
In the year 2016	15,673	16,443	945	33,061	31,275
In the year 2017	14,893	13,113	808	28,814	27,736
In the year 2018	14,752	11,211		25,963	25,000
In the year 2019	14,653	5,010		19,663	18,825
Subsequent	170,568	5,565		176,133	151,780
Total	243,312	73,635	6,322	323,269	332,382

The aircraft lease payments consist of ordinary lease payments not maintenance reserves.

34. Leases as lessor

As a lessor the Company leases aircraft on wet, dry and other various leases, both on short and long term leases. Lease income for the year 2014 amounted to USD 74.8 million (2013; USD 118.0 million). Contracted leases at year end were as follows:

	2014	2013
In the year 2014	-	62,458
In the year 2015	63,987	66,429
In the year 2016	55,190	59,946
In the year 2017	51,619	43,190
In the year 2018	51,511	42,983
In the year 2019	19,777	16,935
Subsequent	18,711	18,711
Total	260,795	310,652

35. Guarantees

IG Invest, a former subsidiary of the Company, has signed an agreement with Boeing for the purchase of one Boeing 787 Dreamliner aircraft to be delivered in the year 2017. Despite the disposal of IG Invest, Icelandair Group is still guarantor for these capital commitments.

As a part of the financial restructuring of the Company's balance sheet in 2010 the Company divested assets to its creditors for USD 59.1 million. Icelandair Group guarantees that the final sale price will be at least USD 31.4 million (ISK 4.0 billion), however the maximum guarantee is USD 3.9 million (ISK 0.5 billion). Based on the managements estimate the Company has fully provided for potential losses due to the guarantee.

36. Capital commitments

In February 2013 Icelandair Group and Boeing finalized an agreement for the purchase of sixteen 737 MAX8 and 737 MAX9 aircraft with an option to purchase additional eight aircraft. The delivery of the first aircraft is scheduled in the first half of 2018. The commitment for all sixteen aircraft was valued at USD 1.6 billion at Boeing list prices when the agreement was finalised. The list price of these aircraft is currently USD 1.755 billion. The Company received acceptable discounts which due to confidentiality agreements cannot be disclosed. Prepayments according to the agreement will be made over the construction period. The Company's plan is to finance the acquisition with internal resources, capital markets and aviation finance products.

Amounts are in USD thousand

Notes, continued:

37. Related parties

Identity of related parties

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

Transactions with management and key personnel

Salaries and benefits of management paid for their service to Group companies and the number of shares in the Company held by management are specified below. Salaries and benefits are presented in ISK, rounded to nearest thousand.

Board of Directors:	2014 Salaries and benefits ISK	Number of shares held at year-end 2014 in thousands	2013 Salaries and benefits ISK	Number of shares held at year-end 2013 in thousands
Sigurður Helgason, Chairman of the Board	8,100	14,000	7,981	14,000
Ásthildur Margrét Otharsdóttir	4,500		4,440	
Katrín Olga Jóhannesdóttir	6,000	413	5,940	413
Magnús Magnússon	2,875*		1,625*	
Úlfar Steindórsson	6,150		6,060	
Elín Jónsdóttir, former board member	1,702			
Herdís Dröfn Fjeldsted, former board member	1,325**		4,290**	
Key employees:				
Björgólfur Jóhannsson CEO of Icelandair Group hf.	45,833	1,300	44,377	1,300
Bogi Nils Bogason, CFO of Icelandair Group hf.	39,795	1,000	36,738	1,000
Birkir Hólm Guðnason, CEO of Icelandair ehf.	39,415		36,903	
Seven MD's of Group companies	192,556	7,111	170,948	7,111

Included in the above mentioned list of shares held by management and directors are shares held by companies controlled by them.

*One board member had waived his rights to salaries, instead the board agreed to contribute equal amounts to Icelandair's Special Children's Travel Fund. From August 2014 the board member started receiving salary.

**The salary of one board member was paid to Framtakssjódur Íslands slhf.

Transaction with associates

During the year 2014 the Group purchased services from associates for USD 0.1 million (2013: USD 0.1 million). The Group's revenues were USD 0.1 million from associates (2013: USD 0.1 million). The Group has not granted repayment of loans for its associates. Transactions with associates are priced on an arm's length basis.

Transaction with shareholders

There are no shareholders with significant influence at year end 2014. Companies which members of the Board and key employees control have been identified as being eleven. These companies have been identified as related. Transactions with them consist of purchase and sale of services in the ordinary course of business on an arm's length basis. Total purchases in 2014 from these entities amounted to USD 0.1 million (2013: USD 0.1 million). Total sales amounted to USD 0.1 million (2013: USD 0.1 million).

Notes, continued:

38. Reassessment of taxes

In December 2013 the Directorate of Internal Revenue ruled that interest expenses on loans that had been transferred to the Company as a result of a reverse acquisition in 2006 did not qualify as tax deductible expenses and reassessed taxes for the years 2007 to 2011. The Company's management does not agree with the reasoning for the ruling and an appeal to the State Internal Revenue Board has been filed. The management is of the opinion that the ruling by the tax authorities will be overruled and the effect of reassessment is therefore not included in the financial statements. If the ruling will however be confirmed the Company's net equity will be reduced by approximately USD 11 million.

39. Group entities

The Company held eleven subsidiaries at year end 2014 which are all included in the consolidated financial statements. They are as follows:

	Ownership interest 2014	Ownership interest 2013
Route network:		
Air Iceland ehf.	100%	100%
Feria ehf.	100%	100%
Fjárvakur - Icelandair Shared Services ehf.	100%	100%
Icelandair ehf.	100%	100%
Icelandair Cargo ehf.	100%	100%
IGS ehf.	100%	100%
Loftleiðir - Icelandic ehf.	100%	100%
Tourism services:		
Iceland Travel ehf.	100%	100%
Icelandair Hotels ehf.	100%	100%
Other operation:		
A320 ehf.	100%	100%
IceCap Ltd., Guernsey	100%	100%

The subsidiaries further own fifteen subsidiaries that are included in the consolidated financial statements. Four of those have non-controlling shareholders.

At year end, shares in the subsidiaries in Route Network and Tourism services are pledged as mortgage against the Group's borrowings.

40. Statement of cash flows

Other operating items in the statement of cash flows are specified as follows:	2014	2013
Expensed deferred cost	20,613	24,852
Exchange rate difference and indexation of liabilities and assets	3,823	3,461
Gain on the sale of operating assets	(204)	(1,100)
Gain on sale of investments	(211)	0
Share of loss of associates	216	38
Income tax	(3,258)	8,017
Total other operating items in the statement of cash flows	20,979	35,268

Amounts are in USD thousand

Notes, continued:

41. Net change in operating assets and liabilities in the statement of cash flows is specified as follows:

	2014	2013
Inventories, increase	(738)	(4,791)
Trade and other receivables, decrease	6,633	22,934
Trade and other payables, increase	25,196	18,910
Deferred income, increase	21,417	31,436
Net change in operating assets and liabilities in the statement of cash flows	52,508	68,489

42. Additional cash flow information:

	2014	2013
Interest paid	6,421	8,081
Interest received	2,213	3,531
Taxes paid	6,708	0

43. Ratios

The Group's primary ratios at year end are specified as follows:

	2014	2013
Current ratio	0.83	0.94
Equity ratio	0.43	0.42
Intrinsic value of share capital	8.99	8.52

Amounts are in USD thousand

Notes, continued:

44. Significant accounting policies

The accounting policies set out in this note have been applied consistently to all periods presented in these consolidated financial statements and have been applied consistently by Group entities.

A number of new standards and amendments to standards are effective for annual periods beginning after 1 January 2014. Of those only IFRS 10 Consolidated Financial Statements and IFRS 12 Disclosure of Interests in Other Entities effect the Group´s financial statements. The Group has adopted these standards but their impact on the Group´s financial statements are immaterial.

a. Basis of consolidation

(i) Subsidiaries

Subsidiaries are entities controlled by the Group. The Group controls an entity when it is exposed to, or has right to, variable returns from its involvement with the entity and has the ability to affect those returns through its power over the entity. The financial statements of subsidiaries are included in the consolidated statements from the date on which control commences until the date on which control ceases.

(ii) Investments in associates

Associates are those entities in which the Group has significant influence, but not control, over the financial and operating policies. Interests in associates are accounted for using the equity method. They are initially recognised at cost, which includes transaction costs. Subsequent to initial recognition, the consolidated financial statements include the Group's share of the profit or loss and other comprehensive income of associates, until the date on which significant influence ceases.

(iii) Transactions eliminated on consolidation

Intra-group balances and transactions, and any unrealised income and expenses arising from intra-group transactions, are eliminated. Unrealised gains arising from transactions with associates are eliminated against the investment to the extent of the Group's interest in the investee. Unrealised losses are eliminated in the same way as unrealised gains, but only to the extent that there is no evidence of impairment

b. Currency exchange

(i) Currency transactions

Transactions in currencies other than functional currencies (foreign currencies) are translated to the respective functional currencies of Group entities at exchange rates at the dates of the transactions. Monetary assets and liabilities denominated in currencies at the reporting date are translated to the functional currency at the exchange rate at that date. The currency gain or loss on monetary items is the difference between amortised cost in the functional currency at the beginning of the year, adjusted for effective interest and payments during the year, and the amortised cost in currency translated at the exchange rate at the end of the year.

Non-monetary assets and liabilities denominated in foreign currencies that are measured at fair value are retranslated to the functional currency at the exchange rate at the date that the fair value was determined. Non-monetary items in a foreign currency that are measured based on historical cost are translated using the exchange rate at the date of the transaction. Foreign currency differences arising on retranslation are recognised in profit or loss, except for differences arising on a financial liability designated as a hedge of the net investment in a foreign operation to the extent that the hedge is effective (see (iii) below), or qualifying cash flow hedges to the extent the hedge is effective, which are recognised in other comprehensive income.

(ii) Subsidiaries with other functional currency

Assets and liabilities of foreign operations and subsidiaries with functional currency in other than USD, including goodwill and fair value adjustments arising on acquisitions, are translated to USD at exchange rates at the reporting date. Income and expenses are translated to USD at exchange rates at the dates of the transactions. Currency differences arising on translation are recognised in other comprehensive income. When an operation is disposed of, in part or in full, the relevant amount in the currency translation reserve within equity is transferred to profit or loss as part of the profit or loss on disposal.

Currency differences are recognised in other comprehensive income, and presented in the translation reserve in equity. However, if the operation is not a wholly owned subsidiary, then the relevant proportion of the translation difference is allocated to the non-controlling interests.

When the settlement of a monetary item receivable from or payable to a foreign operation is neither planned nor likely in the foreseeable future, foreign exchange gains and losses arising from such a monetary item are considered to form part of a net investment in a foreign operation and are recognised in other comprehensive income, and presented in the translation reserve in equity.

(iii) Hedge of net investment in foreign operations

The Group applies hedge accounting to foreign currency differences arising between the functional currency of the subsidiary and the Company's functional currency (USD), regardless of whether the net investment is held directly or through an intermediate parent.

Notes, continued:

44. b. continued:

Currency differences arising on the translation of a financial liability designated as a hedge of a net investment in a subsidiary are recognised in other comprehensive income to the extent that the hedge is effective, and are presented in the translation reserve within equity. To the extent that the hedge is ineffective, such differences are recognised in profit or loss. When the hedged net investment is disposed of, the relevant amount in the translation reserve is transferred to profit or loss as part of the gain or loss on disposal.

c. Financial instruments

(i) Non-derivative financial assets

The Group initially recognises loans and receivables and deposits on the date that they are originated. All other financial assets, including assets designated at fair value through profit or loss, are recognised initially on the trade date, which is the date that the Group becomes a party to the contractual provisions of the instrument.

The Group derecognises a financial asset when the contractual rights to the cash flows from the asset expire, or it transfers the rights to receive the contractual cash flows in a transaction in which substantially all the risks and rewards of ownership of the financial asset are transferred. Any interest in such derecognised financial assets that is created or retained by the Group is recognised as a separate asset or liability.

Financial assets and liabilities are offset and the net amount presented in the statement of financial position when, and only when, the Group has a legal right to offset the amounts and intends either to settle on a net basis or to realise the asset and settle the liability simultaneously.

The Group classifies non-derivative financial assets into the following categories: financial assets at fair value through profit or loss and loans and receivables.

Financial assets at fair value through profit or loss

A financial asset is classified at fair value through profit or loss if it is classified as held-for-trading or is designated as such on initial recognition. Financial assets are designated as at fair value through profit or loss if the Group manages such investments and makes purchase and sale decisions based on their fair value in accordance with the Group's documented risk management or investment strategy. Attributable transaction costs are recognised in profit or loss as incurred. Financial assets at fair value through profit or loss are measured at fair value and changes therein which takes into account any dividend income, are recognised in profit or loss.

Financial assets classified as held-for-trading comprise marketable securities actively managed by the Group's treasury department to address short-term liquidity needs.

Loans and receivables

Loans and receivables are financial assets with fixed or determinable payments that are not quoted in an active market. Such assets are recognised initially at fair value plus any directly attributable transaction costs. Subsequent to initial recognition, loans and receivables are measured at amortised cost using the effective interest method, less any impairment losses.

Loans and receivables comprise restricted cash and cash equivalents and trade and other receivables.

Cash and cash equivalents

Cash and cash equivalents comprise cash balances and call deposits and marketable securities with original maturities of three months or less from the acquisition date that are subject to an insignificant risk of changes in their fair value, and are used by the Group in the management of its short-term commitments.

(ii) Non-derivative financial liabilities

The Group initially recognises debt securities issued on the date that they are originated. All other financial liabilities including liabilities designated at fair value through profit or loss are recognised initially on the trade date, which is the date that the Group becomes a party to the contractual provisions of the instrument.

The Group derecognises a financial liability when its contractual obligations are discharged, cancelled or expire.

The Group classifies non-derivative financial liabilities into the other financial liabilities category. Such financial liabilities are recognised initially at fair value less any directly attributable transaction costs. Subsequent to initial recognition, these financial liabilities are measured at amortised cost using the effective interest method. Other financial liabilities comprise loans and borrowings and trade and other payables.

Notes, continued:

44. c. continued:

(iii) Share capital

Ordinary shares

Ordinary shares are classified as equity. Incremental costs directly attributable to the issue of ordinary shares are recognised as a deduction from equity, net of any tax effects.

Repurchase and reissue of share capital

When share capital recognised as equity is repurchased, the amount of the consideration paid, which includes directly attributable costs, net of any tax effects, is recognised as a deduction from equity. Repurchased shares are classified as treasury shares and are presented as a deduction from total equity. When treasury shares are sold or reissued subsequently, the amount received is recognised as an increase in equity, and the resulting surplus or deficit on the transaction is presented in share premium.

(iv) Derivative financial instruments, including hedge accounting

The Group holds derivative financial instruments to hedge its foreign currency, fuel price and interest rate risk exposures (see note 32). Derivatives are recognised initially at fair value; attributable transaction costs are recognised in profit or loss as incurred. Subsequent to initial recognition, derivatives are measured at fair value, and changes therein are accounted for as described below. The Group holds no trading derivatives.

On initial designation of the derivative as a hedging instrument, the Group formally documents the relationship between the hedging instrument and hedged item, including the risk management objectives and strategy in undertaking the hedge transaction and the hedged risk, together with the methods that will be used to assess the effectiveness of the hedging relationship. The Group makes an assessment, both at the inception of the hedge relationship as well as on an ongoing basis, whether the hedging instruments are expected to be highly effective in offsetting the changes in the fair value or cash flows of the respective hedged items during the period for which the hedge is designated, and whether the actual results of each hedge are within a range of 80-125 percent. For a cash flow hedge of a forecast transaction, the transaction should be highly probable to occur and should present an exposure to variations in cash flows that ultimately could affect reported profit or loss.

Cash flow hedges

When a derivative is designated as the hedging instrument in a hedge of the variability in cash flows attributable to a particular risk associated with a recognised asset or liability or a highly probable forecast transaction that could affect profit or loss, the effective portion of changes in the fair value of the derivative is recognised in other comprehensive income and presented in the hedging reserve in equity. Any ineffective portion of changes in the fair value of the derivative is recognised immediately in profit or loss.

When the hedged item is a non-financial asset, the amount accumulated in equity is included in the carrying amount of the asset when the asset is recognised. In other cases the amount accumulated in equity is reclassified to profit or loss in the same period during which the hedged item affects profit or loss. If the hedging instrument no longer meets the criteria for hedge accounting, expires or is sold, terminated or exercised, or the designation is revoked, then hedge accounting is discontinued prospectively. If the forecast transaction is no longer expected to occur, then the balance in equity is reclassified in profit or loss.

Other non-trading derivatives

When a derivative financial instrument is not designated in a hedge relationship that qualifies for hedge accounting, all changes in its fair value are recognised immediately in profit or loss.

d. Operating assets

(i) Recognition and measurement

Items of operating assets are measured at cost less accumulated depreciation and accumulated impairment losses.

Cost includes expenditure that is directly attributable to the acquisition of the asset. The cost of self-constructed assets includes the cost of materials and direct labour, any other costs directly attributable to bringing the assets to a working condition for their intended use.

When parts of an item of operating assets have different useful lives, they are accounted for as separate items (major components) of operating assets.

Notes, continued:

44. d. continued:

Any gain and loss on disposal of an item of operating assets (calculated as the difference between the net proceeds from disposal and the carrying amount of the item) is recognised in profit or loss.

(ii) Aircraft and flight equipment

Aircraft and flight equipment, e.g. aircraft engines and aircraft spare parts, are measured at cost less accumulated depreciation and accumulated impairment losses. When an aircraft is acquired the purchase price is divided between the aircraft itself and engines. Aircraft is depreciated over the estimated useful life of the relevant aircraft until a residual value is met. Engines are depreciated according to actual usage based on cycles flown. When an engine is overhauled the cost of the overhaul is capitalised and the remainder of the cost of the previous overhaul that has not already been depreciated, if any, is expensed in full.

(iii) Subsequent costs

Subsequent expenditure is capitalised only when it is probable that the future economic benefits associated with the expenditure will flow to the Group. Ongoing repairs and maintenance is expensed as incurred.

(iv) Depreciation

Depreciation is based on the cost of an asset less its residual value. Significant components of individual assets are assessed and if a component has a useful life that is different from the remainder of that asset, that component is depreciated separately.

Items of operating assets are depreciated on a straight-line basis in profit or loss over the estimated useful lives of each component unless other systematic method is considered appropriate. Leased assets are depreciated over the shorter of the lease term or their useful lives. The estimated useful lives for the current and comparative periods are as follows:

	Useful life
Aircraft and flight equipment	3-17 years
Engines	Cycles flown
Buildings	17-50 years
Other property and equipment	3-20 years

Depreciation methods, useful lives and residual values are reviewed at each reporting date and adjusted if appropriate.

e. Intangible assets and goodwill

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

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

Goodwill is measured at cost less accumulated impairment losses. Goodwill is allocated to cash-generating units and is tested annually for impairment.

Negative goodwill arising on an acquisition is recognised directly in profit or loss.

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

(ii) Other intangible assets

Other intangible assets acquired by the Group and have finite useful lives are measured at cost less accumulated amortisation and accumulated impairment losses. Amortisation is recognised in profit or loss on a straight-line basis over the estimated useful lives since this most closely reflects the expected pattern of consumption of the future economic benefits embodied in the asset. The estimated useful lives for the current and comparative years are as follows:

	Useful life
Software	3 years
Customer relations	7-10 years
Other intangible assets	6-10 years

Amortisation methods, useful lives and residual values are reviewed at each reporting date and adjusted if appropriate.

Notes, continued:

44. e. continued:

(iii) Subsequent expenditure

Subsequent expenditure is capitalised only when it increases the future economic benefits embodied in the specific asset to which it relates. All other expenditure, including expenditure on internally generated goodwill and brands, is recognised in profit or loss as incurred.

f. Leased assets

All leases are operating leases and the leased assets are not recognised in the Group's statement of financial position.

g. Inventories

Goods for resale and supplies are measured at the lower of cost and net realisable value. The cost of inventories is based on first-in first-out principle and includes expenditure incurred in acquiring the inventories and bringing them to their existing location and condition. Net realisable value is the estimated selling price in the ordinary course of business, less the estimated costs of completion and selling expenses.

h. Impairment

(i) Non-derivative financial assets

A financial asset not carried at fair value through profit or loss is assessed at each reporting date to determine whether there is objective evidence that it is impaired. A financial asset is impaired if there is objective evidence of impairment as a result of one or more events has occurred after the initial recognition of the asset, and that loss events had an impact on the estimated future cash flows of that asset that can be estimated reliably.

An impairment loss in respect of a financial asset measured at amortised cost is calculated as the difference between its carrying amount and the present value of the estimated future cash flows discounted at the asset's original effective interest rate. Losses are recognised in profit or loss and reflected in an allowance account against receivables. Interest on the impaired asset continues to be recognised. When an event occurring after the impairment recognised causes the amount of impairment loss to decrease, the decrease in impairment loss is reversed through profit or loss.

(ii) Non-financial assets

The carrying amounts of the Group's non-financial assets, other than inventories and deferred tax assets, are reviewed at each reporting date to determine whether there is any indication of impairment. If any such indication exists, then the asset's recoverable amount is estimated. Goodwill and indefinite-lived intangibles assets are tested annually for impairment. An impairment loss is recognised if the carrying amount of an asset or cash-generating unit (CGU) exceeds its recoverable amount.

The recoverable amount of an asset or CGU is the greater of its value in use and its fair value less costs to sell. In assessing value in use, the estimated future cash flows are discounted to their present value using a pre-tax discount rate that reflects current market assessments of the time value of money and the risks specific to the asset or CGU. For the purpose of impairment testing, assets that cannot be tested individually are grouped together into the smallest group of assets that generates cash inflows from continuing use that are largely independent of the cash inflows of other assets or CGUs. Subject to an operating segment ceiling test, for the purposes of goodwill impairment testing, CGUs to which goodwill has been allocated are aggregated so that the level at which impairment testing is performed reflects the lowest level at which goodwill is monitored for internal reporting purposes. Goodwill acquired in a business combination is allocated to groups of CGUs that are expected to benefit from the synergies of the combination.

Impairment losses are recognised in profit or loss. Impairment losses recognised in respect of CGUs are allocated first to reduce the carrying amount of any goodwill allocated to the CGU (group of CGUs), and then to reduce the carrying amounts of the other assets in the CGU (group of CGUs) on a pro rata basis.

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

Notes, continued:

44. h. continued:

The Group's corporate assets do not generate separate cash inflows and are utilised by more than one CGU. Corporate assets are allocated to CGUs on a reasonable and consistent basis and tested for impairment as part of the testing of the CGU to which the corporate asset is allocated.

An impairment loss in respect of goodwill is not reversed. For other assets, an impairment loss is reversed only to the extent that the asset's carrying amount does not exceed the carrying amount that would have been determined, net of depreciation or amortisation, if no impairment loss had been recognised.

i. Provisions

A provision is recognised if, as a result of a past event, the Group has a present legal or constructive obligation that can be estimated reliably and it is probable that an outflow of economic benefits will be required to settle the obligation. Provisions are determined by discounting the expected future cash flows at a pre-tax rate that reflects current market assessments of the time value of money and the risks specific to the liability.

Overhaul commitments relating to aircraft under operating lease

With respect to the Group´s operating lease agreements, where the Group has a commitment to maintain the aircraft, provision is made during the lease term for the obligation based on estimated future cost of major airframe and certain engine maintenance checks by making appropriate charges to the profit or loss calculated by reference to the number of hours or cycles operated.

Provisions are entered into the statement of financial position among non-current and current payables, as applicable.

j. Deferred income

Sold unused tickets, fair value of unutilized frequent flyer points and other prepayments are presented as deferred income in the statement of financial position.

Icelandair's frequent flyer program

Frequent flyer points earned or sold are accounted for as a liability on a fair value basis of the services that can be purchased for the points. The points are recognized as revenue when they are utilized or when they expire.

k. Operating income

(i) Transport revenue

Passenger ticket sales are not recognised as revenue until transportation has been provided. Sold refundable documents not used within twelve months from the month of sale are recognised as revenue. Non-refundable documents are recognized as revenue two months after expected transport if not used. Revenue from mail and cargo transportation is recognised when transportation has been provided.

(ii) Customer loyalty programmes

For customer loyalty programmes, the fair value of the consideration received or receivable in respect of the initial sale is allocated between the award credits (frequent flyer points) and the other components of the sale. Awards can also be generated through transportation services supplied by the Group. Through transportation services the amount allocated to the points is estimated by reference to the fair value of the services for which they could be redeemed, since the fair value of the points themselves is not directly observable. The fair value of the services is estimated taking into account the expected redemption rate and the timing of such expected redemptions. Such amount is deferred and revenue is recognised only when the points are redeemed and the Group has fulfilled its obligations to supply the services. The amount of revenue recognised in those circumstances is based on the number of points that have been redeemed in exchange for services, relative to the total number of points that is expected to be redeemed.

(iii) Aircraft and aircrew lease

Revenue from aircraft and aircrew lease is recognised in profit or loss when the service has been provided.

(iv) Other operating revenue

Revenue includes revenue from tourism, sales at airports and hotels, maintenance service sold and other revenue. Revenue is recognised in profit or loss when the service has been provided or sale completed by delivery of products.

Gain on sale of operating assets is recognised in profit or loss when the risks and rewards of ownership are transferred to the buyer.

Notes, continued:

44. k. continued:

l. Employee benefits

(i) Short-term employee benefits

Short-term employee benefits are expensed as the related service is provided. A liability is recognised for the amount expected to be paid if the Group has a present legal or constructive obligation to pay this amount as a result of past service provided by the employee and the obligation can be estimated reliably.

(ii) Defined contribution plans

Obligations for contributions to defined contribution plans are expensed as the related service is provided.

m. Lease payments

Operating lease payments

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

n. Finance income and finance costs

Finance income comprises interest income on funds invested, dividend income, foreign currency gains, and gains on hedging instruments that are recognised in profit or loss. Interest income is recognised as it accrues in profit or loss, using the effective interest method. Dividend income is recognised in profit or loss on the date that the Group´s right to receive payment is established.

Finance costs comprise interest expense on borrowings, unwinding of the discount on provisions, foreign currency losses, impairment losses recognised on financial assets, and losses on hedging instruments that are recognised in profit or loss. Borrowing costs that are not directly attributable to the acquisition of a qualifying asset are recognised in profit or loss using the effective interest method.

Foreign currency gains and losses are reported on a net basis as either finance income or finance cost depending on whether currency movements are in a net gain or net loss position.

o. Income tax

Income tax expense comprises current and deferred tax. It is recognised in profit or loss except to the extent that it relates to items recognised directly in equity or in other comprehensive income.

Current tax is expected tax payable on the taxable income for the period, using tax rates enacted at the reporting date.

Current tax comprises the expected tax payable on the taxable income for the year. It is measured using tax rates enacted at the reporting date.

Deferred tax is recognized in respect of temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for taxation purposes. Deferred tax is not recognized for goodwill not deductible for tax purposes, the initial recognition of assets or liabilities that do not affect accounting, or taxable profit or differences relating to investment in subsidiaries.

A deferred tax asset is recognized for unused tax losses and deductible temporary differences, to the extent that it is probable that future taxable profits will be available against which they can be used. Deferred tax assets are reviewed at each reporting date and are reduced to the extent that it is no longer probable that the related tax benefit will be realized.

Deferred tax is measured at the tax rates that are expected to be applied to temporary differences when they reverse, using tax rates enacted at the reporting date.

Notes, continued:

44. continued:

p. Earnings per share

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

q. Segment reporting

An operating segment is a component of the Group that engages in business activities from which it may earn revenue and incur expenses, including revenue and expenses that relate to transactions with any of the Group's other components. An operating segment's operating results are reviewed regularly by the CEO to make decisions about resources to be allocated to the segment and assess its performance, and for which discrete financial information is available. The major revenue-earning assets of the Group is the aircraft fleet, the majority of which is registered in Iceland. Since the Group's aircraft fleet is employed flexibly across its route network, there is no suitable basis of allocating such assets and related liabilities to geographical segments.

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

Segment results, reported to the CEO include items directly attributable to a segment as well as those that can be allocated on a reasonable basis. Unallocated items comprise mainly investments and related revenue, loans and borrowings and related expenses, corporate assets and head office expenses, and income tax assets and liabilities.

Corporate Governance Statement

The framework

The guidelines on Corporate Governance issued by the Iceland Chamber of Commerce, NASDAQ OMX Iceland and the Confederation of Icelandic Employers, along with the Company's Articles of Association, and rules for Issuers of Securities listed on the NASDAQ OMX Iceland, make up the framework for Icelandair Group's Corporate Governance practices. The Company's Articles of Association are on the Company's website and the guidelines and the rules for Issuers are on the website of NASDAQ OMX Iceland.

The Company complies in all main respect to the rules mentioned above. The Company however does not have a Nomination Committee as the Board of Directors has not seen the need for it. No government organization has found the Company to be in breach with any rule or regulation regarding corporate governance.

In 2012 The Iceland Chamber of Commerce, the Confederation for Icelandic Employers and Nasdaq OMX Iceland hf. granted the Company a recognition for “Exemplary in corporate governance”. The aim with the recognition is to increase credibility and transparency of Icelandic companies' corporate governance with respect to shareholders and interested parties.

Internal audit and risk management

The Group's Audit Committee oversees how management monitors compliance with the Group's risk management policies and procedures and reviews the adequacy of the risk management framework in relation to the risks faced by the Group. The Group's Audit Committee is assisted in its oversight role by Internal Audit. Internal Audit undertakes both regular and ad hoc reviews of risk management controls and procedures, the results of which are reported to the Audit Committee. The committee shall oversee the annual accounts of the Company and the Group's consolidated accounts. The committee is responsible for evaluation of the independence and the eligibility of both the Company´s auditor and auditing firm. The committee shall make suggestions to the Board of Directors regarding the selection of the Company´s auditor. The Audit Committee held eight meetings in 2014.

Audit Committee:
Katrín Olga Jóhannesdóttir, Chairman
Ásthildur Margrét Otharsdóttir
Magnús Magnússon

Values and code of ethics and corporate responsibility

The company's values are:
WE CARE for our customers, employees, environment and shareholders.
WE THINK CLIENTS through consistency, reliability, clear product alternatives and friendly service.
WE DRIVE RESULTS via teamwork, shared information and values, accountability and profitability.

On 25 May 2009 the Board of Directors approved a Code of Ethics that was amended on 5 January 2011. The Code of Ethics is accessible to all Company's employees through the Company's intranet, MyWork.

Compensation Committee

The purpose of the Compensation Committee is to avoid placing the Company's management in control of their own remuneration and, furthermore, to ensure that the management's remuneration is structured so as to serve the long-term interests of shareholders. The main tasks of the Compensation Committee are policy making with respect to the management's performance related bonuses, including stock options. The Committee conducts evaluations of management remuneration and monitors the management's acquisition of stock in the Company. The Compensation Committee meets on average four times a year.

Compensation Committee
Sigurður Helgason, Chairman
Úlfar Steindórsson

Corporate Governance Statement, continued:

The Board of Directors and Executive Committee
Board of Directors
Sigurður Helgason, Chairman
Sigurður Helgason was born in 1946. He was President & CEO of Flugleidir/FL-Group/Icelandair 1985 - 2005. He was Director of Cash Management 1974-1980, Senior Vice-President of Finance 1980-1983 and General Manager of The Americas 1983-1985 for Flugleidir/Icelandair. He was Chairman of the Board of The Icelandic International Development Fund 2005-2008. He is the Chairman of the Icelandair Special Children Travel Fund since 2005. He was a member of the IATA board of Governors 2004/2005. He graduated with a MBA degree from The University of North Carolina, Chapel Hill, USA in 1973 and a Cand. Oecon. degree from the University of Iceland in 1971. He joined the Board on 6 August 2009.

Úlfar Steindórsson, Deputy Chairman
Úlfar Steindórsson was born in 1956 and is CEO of Toyota in Iceland ehf. and Jú ehf. He was CEO of Primex ehf in Siglufjordur from 2002-2004, and CEO of the New Business Venture Fund from 1999-2002. Úlfar is chairman of the board of Eignarhalds-félagið Bifreiðar ehf., Bergey ehf., Bifreiðainnflutningur ehf., Bílaútleigan ehf., Okkar bílaleiga ehf., and TK bílar ehf. He is a Board member of Toyota á Íslandi ehf, Króksslóð ehf, TMH Iceland ehf, AB 257 ehf, Blue Lagoon international ehf., Eldvörp ehf., Hótel Bláa lónið ehf., Bláa Lónið Heilsuvörur ehf., UK fjárfestingar ehf, Johan Rönning hf, S.Guðjónsson ehf., Skorri ehf., and UK fjárfestingar ehf. Úlfar holds a Cand. Oecon degree from the University of Iceland and an MBA from Virginia Commonwealth University. He joined the Board on 15 September 2010.

Ásthildur Margrét Otharsdóttir
Ásthildur was born in 1968 and is an independent management consultant with prior business experience as Global Director of Treasury and Corporate Development at Össur hf., Senior Account Manager at Kaupthing Bank hf. and Management Consultant at Accenture in Copenhagen. She is Chairman of the Board of Directors of Marel hf. and JÖR ehf. Ásthildur is a member of the Board of Directors of Marorka ehf.,and the Research Center for Business Ethics at the University of Iceland and the Court of Arbitration of the Icelandic Chamber of Commerce. Ásthildur has an MBA degree from the Rotterdam School of Management, Erasmus University and a Cand. Oecon degree from the University of Iceland. She joined the Board on 23 March 2012.

Katrín Olga Jóhannesdóttir
Katrín Olga Jóhannesdóttir was born in 1962 and is the former Chief Strategy Officer of Skipti hf. and the current Chairman of Já upplýsingaveitur hf. Before that she was VP for sales and marketing and VP for residential markets at Síminn hf. Prior to that she held a position as the Managing Director of Navision Iceland and was a management consultant at VSO. Katrín Olga currently serves on the Boards of Directors of Ölgerðin hf., Reykjavik University, the Iceland Chamber of Commerce Advania and Njála ehf., having previously served on the Boards of the Central Bank of Iceland., Sirius IT and SkjáMiðlar. She holds a Cand. Oecon degree from the University of Iceland and an M.Sc. in Business Economics from Odense University. She joined the Board on 6 August 2009.

Magnús Magnússon
Magnús has been employed as a division manager at LBI hf. since early 2009, having previously worked for Búnadarbankinn and the financing company Lýsing following a period of self-employment from 2003 to year-end 2008. Magnús currently serves on the Boards of Directors of Lýsi hf. and the manufacturing and contracting company Loftorka in Borgarnes, as well as several subsidiaries of LBI hf. Magnús holds a degree in Business Economics from the University of Iceland and a Masters Degree in international business from Norges Handelshøyskole. Magnús has been a reserve member of Icelandair Group's Board of Directors since 2009 and a member of the Board since fall 2014.

Corporate Governance Statement, continued:

Executive committee

Björgólfur Jóhannsson, president and CEO

Björgólfur was born in 1955 and joined Icelandair Group on 15 January 2008. Before joining Icelandair Group, Björgólfur was the CEO of Icelandic Group hf. from March 2006. From 1992-1996 Björgólfur was the CFO of UA in Akureyri. He became the CEO of Síldarvinnslan hf. in 1999 and served as the Director of Innovation and Development at Samherji hf. from 1996, having worked as a chartered accountant for two auditing firms from 1980. Björgólfur served as the Chairman of the Board of the Federation of Icelandic Fishing Vessel Owners from 2003-2008. Björgólfur is the Chairman of the Confederation of Icelandic Employers and a Board member of the Iceland Chamber of Commerce. He graduated with a degree in Business Administration from the University of Iceland in 1983 and became a chartered accountant in 1985.

Bogi Nils Bogason, CFO
Birkir Hólm Guðnason, CEO of Icelandair
Magnea Þórey Hjálmarsdóttir, Managing Director of Icelandair Hotels

Board of Directors

The Company's Board of Directors exercises the supreme authority in the Company's affairs between shareholders' meetings, and it is entrusted with the task of ensuring that the organisation and activities of the Company's operation are at all times in correct and proper order.

The Board of Directors is instructed in the Company's Articles of Association to appoint a President and CEO for the Company and decide the terms of his or her employment. The Board of Directors and President and CEO are responsible for the management of the Company.

The Company's Board of Directors must at all times ensure that there is adequate supervision of the Company's accounts and the safeguarding of its assets and shall adopt working procedures in compliance with the Companies Act. Only the Board of Directors may assign powers of procuration on behalf of the Company. The signatures of the majority of the members of the Board are required to bind the Company. The President and CEO has charge of the day-to-day operation of the Company and is required in his work to observe the policy and instructions set out by the Company's Board of Directors. Day-to-day operation does not include measures which are unusual or extraordinary. Such measures can only be taken by the President and CEO with the specific authorization of the Board of Directors, unless it is impossible to await the decision of the Board without seriously disadvantaging the operation of the Company. In such instances, the President and CEO is required to consult with the Chairman of the Board, if possible, after which the Board of Directors must immediately be notified of the measures. The President and CEO shall ensure that the accounts and finances of the Company conform to the law and accepted practices and that all assets belonging to the Company are securely safeguarded. The President and CEO is required to 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.

The Company's Board of Directors consists of five 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 must 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 scheduled. Only those who have informed the Board of their candidacy are eligible.

Corporate Governance Statement, continued:

The Board of Directors elects a Chairman and Deputy Chairman from its members, and otherwise allocates its obligations among its members as needed. The Chairman calls Board meetings. A meeting must also be held if requested by a member of the Board of Directors or the President and CEO. Meetings of the Board are valid if attended by a majority of its members. However, important decisions shall not be taken unless all members of the Board have had an opportunity to discuss the matter, if possible. The outcome of issues is decided by force of vote, and in the event of an equality of votes, the issue is regarded as rejected. The President and CEO attends meetings of the Board of Directors, even if he or she is not a member of the Board, and has the right to participate in discussions and submit proposals unless otherwise decided by the Board in individual cases. A book of minutes is kept of proceedings at meetings and must be signed by participants in the meeting. A Board member who disagrees with a decision made by the Board of Directors is entitled to have his or her dissenting opinion entered in the book of minutes. The same applies to the President and CEO. The Chairman is responsible for the Board's relations with the shareholders and he shall inform the Board on the views of the shareholders.

On 12 September 2007 the Board of Directors approved Rules on Working Procedures for the Board of Directors that was emended on 10 August 2012. The Rules on Working Procedures are accessible to the Board of Directors and the management through the Board's intranet, Coredata. In accordance with article 14 of the Rules on Working Procedures the Board of Directors must annually evaluate its work, size, composition and practices, and must also evaluate the performance of the CEO and others responsible for the day-to-day management of the Company and its development. The annual performance assessment is intended to improve working methods and increase the efficiency of the Board. The assessment entails e.g. evaluation of the strengths and weaknesses of the Board's work and practices and takes into consideration the work components which the Board believes may be improved.

The Board of Directors elects the members of the two sub-committees; the Compensation Committee and the Audit Committee. The sub-committees adhere to the Rules on Working Procedures. The Board of Directors convened eighteen times in the year and all Board Members attended almost all meetings. All the Members of the Board of Directors are independent from the Company, except Ásthildur Margrét Otharsdóttir. All Board members were independent of the Company's major shareholders in 2014.

Quarterly statements (unaudited)

Unaudited summary of the Group's operating results by quarters:

Year 2014	**Q1**	**Q2**	**Q3**	**Q4**	**Total**
Operating income	191,277	297,793	418,746	205,481	1,113,297
Operating expenses without depreciation	(204,581)	(252,553)	(294,863)	(206,962)	(958,959)
Operating (loss) profit before depreciation (EBITDA)	(13,304)	45,240	123,883	(1,481)	154,338
Depreciation	(17,296)	(19,390)	(21,368)	(17,275)	(75,329)
Operating (loss) profit (EBIT)	(30,600)	25,850	102,515	(18,756)	79,009
Net finance income (expense)	(2,687)	(1,076)	3,646	1,232	1,115
Share of (loss) profit of associates	(75)	2	28	(171)	(216)
(Loss) profit before income tax	(33,362)	24,776	106,189	(17,695)	79,908
Income tax	6,641	(4,976)	(20,388)	3,240	(15,483)
(Loss) profit from continuing operations	(26,721)	19,800	85,801	(14,455)	64,425
Profit from discontinued operation	0	2,593	0	(519)	2,074
(Loss) profit	(26,721)	22,393	85,801	(14,974)	66,499
Other comprehensive (loss) profit	(1,548)	2,331	(5,737)	(23,578)	(28,532)
Total comprehensive (loss) income	(28,269)	24,724	80,064	(38,552)	37,967
Working capital (used in) from operations	(12,549)	50,270	135,211	(10,125)	162,807
Net cash from operating activities	121,371	83,625	5,767	4,552	215,315
Net cash used in investing activities	(33,946)	(14,009)	(38,383)	(43,818)	(130,156)
Net cash used in financing activities	(29,138)	(52,916)	(3,622)	(3,008)	(88,684)

Year 2013					
Operating income	173,045	265,600	371,662	212,650	1,022,957
Operating expenses without depreciation	(181,359)	(222,664)	(269,421)	(205,803)	(879,247)
Operating (loss) profit before depreciation (EBITDA)	(8,314)	42,936	102,241	6,847	143,710
Depreciation	(14,684)	(18,167)	(20,073)	(17,775)	(70,699)
Operating (loss) profit (EBIT)	(22,998)	24,769	82,168	(10,928)	73,011
Net finance income (expense)	29	(1,409)	(306)	(239)	(1,925)
Share of profit (loss) of associates	46	(55)	(11)	(18)	(38)
(Loss) profit before income tax	(22,923)	23,305	81,851	(11,185)	71,048
Income tax	4,634	(4,815)	(16,526)	2,077	(14,630)
(Loss) profit	(18,289)	18,490	65,325	(9,108)	56,418
Other comprehensive income (loss)	1,549	(777)	1,756	2,964	5,492
Total comprehensive (loss) income	(16,740)	17,713	67,081	(6,144)	61,910
Working capital (used in) from operations	(1,481)	48,154	111,138	4,574	162,385
Net cash from (used in) operating activities	78,453	106,436	30,272	15,713	230,874
Net cash used in investing activities	(40,795)	(15,477)	(24,288)	(32,663)	(113,223)
Net cash used in financing activities	(11,239)	(15,690)	(10,361)	(7,942)	(45,232)

Amounts are in USD thousand

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