Icelandair Group hf.

Condensed Consolidated
Interim Financial Statements
1 January - 31 March 2007

ISK

Icelandair Group hf.
Reykjavíkurflugvöllur
101 Reykjavík
Iceland
Reg. no. 631205-1780

Contents

Endorsement and Signatures of the Board of Directors and the CEO

The condensed consolidated interim financial statements of Icelandair Group hf. for the period from 1 January to 31 March 2007 have been prepared in accordance with International Financial Reporting Standards (IFRSs) for Interim Financial Statements (IAS 34). The interim financial statements comprise the consolidated interim financial statements of Icelandair Group hf. and its subsidiaries, which were twelve at the end of March 2007.

According to the income statement net loss for the period from 1 January to 31 March 2007 amounted to ISK 1,229 million. According to the balance sheet, equity at the end of the period amounted to ISK 24,051 million, including share capital in the amount of ISK 989 million.

On 14 May the Company announced it had signed a letter of intent for acquisition of the Czech airline Travel Service, the largest private airline in the Czech Republic. Travel Service operates charter flights to and from Prague and Budapest and also owns and operates the low cost airline Smart Wings. Under the agreement Icelandair Group hf. will purchase 50% of the shares before the end of June and the remaining 50% during 2008. The signing of the final purchase agreement is planned around mid June 2007.

The Board of Directors and the CEO of Icelandair Group hf. hereby confirm the Company's consolidated interim financial statements for the period from 1 January to 31 March 2007 by means of their signatures.

Reykjavík, 15 May 2007.

Board of Directors:

Finnur Ingólfsson
Ómar Benediktsson
Gunnlaugur M. Sigmundsson
Helgi S. Guðmundsson
Hermann S. Guðmundsson
Jóhann Magnússon

Guðsteinn Einarsson
Jón Benediktsson
Martha Eiríksdóttir

CEO:

Jón Karl Ólafsson

Independent Auditors' Review Report

To the Board of Directors of Icelandair Group hf.

Introduction

We have reviewed the accompanying condensed consolidated interim balance sheet of Icelandair Group hf. as of 31 March 2007 and the related statements of income, changes in equity and cash flows for the three-month period then ended and a summary of significant accounting policies and other explanatory notes. Management is responsible for the preparation and fair presentation of this interim financial information in accordance with International Financial Reporting Standard IAS 34, Interim Financial Reporting. Our responsibility is to express a conclusion on this interim financial information based on our review.

We have also reviewed the pro forma interim financial information presented in the consolidated income statement and consolidated statement of cash flows and the related disclosures made in the notes to these consolidated interim financial statements, which have been compiled on the basis described in note c to these consolidated interim financial statements, for illustrative purposes only, to provide information about how the Group's operations and cash flows might have been if the acquisition of Icelandair Group hf. had been effected at the beginning of the year 2006.

Scope of review

We conducted our review in accordance with International Standard on Review Engagements 2410, "Review of Interim Financial Information Performed by the Independent Auditor of the Entity." A review of interim financial information consists of making inquiries, primarily of persons responsible for financial and accounting matters, and applying analytical and other review procedures. A review is substantially less in scope than an audit conducted in accordance with International Standards on Auditing and consequently does not enable us to obtain assurance that we would become aware of all significant matters that might be identified in an audit. Accordingly, we do not express an audit opinion.

Conclusion

Based on our review, nothing has come to our attention that causes us to believe that the accompanying consolidated interim financial information does not give a true and fair view of the financial position of the entity as at 31 March 2007, and of its financial performance and its cash flows for the three-month period then ended, in accordance with IAS 34, Interim Financial Reporting

In our opinion, the pro forma interim financial information has been properly compiled on the basis stated in note c to these consolidated interim financial statements. Without qualifying our opinion, we draw attention to note c, which states that the pro forma interim financial information is not necessarily indicative of the operations and cash flows that would have been attained if the acquisition of Icelandair Group hf. had indeed taken place at the beginning of the year 2006.

Reykjavík, 15 May 2007

KPMG hf.

Jón S. Helgason
Sæmundur Valdimarsson

Consolidated Income Statement
for the period from 1 January to 31 March 2007

	Notes	2007 1.1.-31.3.	**Pro forma** 2006 1.1.-31.3.
Operating income:			
Transport revenue		6.315	5.555
Aircraft and aircrew lease		2.613	2.217
Other operating revenue		2.977	1.823
		11.905	9.595
Operating expenses:			
Salaries and other personnel expenses		4.602	3.840
Aircraft fuel		1.679	1.654
Aircraft and aircrew lease		1.436	875
Aircraft servicing, handling and communication		738	608
Aircraft maintenance expenses		1.027	695
Other operating expenses		2.504	2.188
		11.986	9.860
Operating loss before depreciation (EBITDA)		(81)	(265)
Depreciation and amortisation		(752)	(867)
Operating loss before net finance (costs) income (EBIT)		(833)	(1.132)
Net finance (costs) income	2	(769)	406
Share of profit of associates		61	9
Loss before income tax		(1.541)	(717)
Income tax		312	129
Loss for the period		(1.229)	(588)
Attributable to:			
Equity holders of the Company		(1.230)	(588)
Minority Interest		1	0
Loss for the period		(1.229)	(588)
Earnings per share:			
Basic earnings per share (ISK)		(1,23)	(0,19)
Diluted earnings per share (ISK)		(1,23)	(0,19)

Interim Financial Statements of Icelandair Group hf. 31 March 2007 Amounts are in ISK million

Consolidated Balance Sheet
as at 31 March 2007

	Notes	31.3.2007	31.12.2006
Assets:			
Operating assets		21.606	22.935
Intangible assets		27.437	27.845
Investments in associates		2.212	2.058
Prepaid aircraft acquisitions		252	9.669
Long-term receivables and deposits		2.632	2.689
Total non-current assets		54.139	65.196
Inventories		1.125	1.131
Trade and other receivables		7.041	6.149
Receivables from sale of aircrafts	3	11.665	1.094
Prepayments		470	271
Cash and cash equivalents		1.233	2.776
Total current assets		21.534	11.421
Total assets		75.673	76.617
Equity:			
Share capital		989	1.000
Share premium		25.793	26.090
Reserves		(1.000)	(584)
Accumulated deficit		(1.774)	(544)
Total equity attributable to equity holders of the Company		24.008	25.962
Minority interest		43	42
Total equity		24.051	26.004
Liabilities:			
Loans and borrowings		16.547	21.607
Deferred income tax liability		484	360
Total non-current liabilities		17.031	21.967
Loans and borrowings		10.783	4.614
Loans to finance prepaid aircraft acquisition		6.732	8.545
Trade and other payables		10.813	12.428
Deferred income		6.263	3.059
Total current liabilities		34.591	28.646
Total liabilities		51.622	50.613
Total equity and liabilities		75.673	76.617

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Consolidated Statement of Changes in Equity
for the period from 1 January to 31 March 2007

	Attributable to equity holders of the Company								
			Reserves						
	Share capital	Share premium	Share option reserve	Hedging reserve	Translation reserve	Accumulated deficit	Total	Minority Interest	Total equity
Equity 1.1.2007	1.000	26.090	0	(159)	(425)	(544)	25.962	42	26.004
Foreign currency translation differences for foreign operations					(708)		(708)		(708)
Net profit on hedge of net investment in foreign operation					9		9		9
Effective portion of changes in fair value of cash flow hedges, net of tax				234			234		234
Net income and expense recognised directly in equity				234	(699)	0	(465)	0	(465)
Loss for the period						(1.230)	(1.230)	1	(1.229)
Total recognised income				234	(699)	(1.230)	(1.695)	1	(1.694)
Own shares, change	(11)	(297)					(308)		(308)
Stock options			49				49		49
Equity 31.3.2007	989	25.793	49	75	(1.124)	(1.774)	24.008	43	24.051

Amounts are in ISK million

Consolidated Statement of Cash Flows for the Three Months Ended 31 March 2007

	Notes	2007 1.1.-31.3.	Pro forma 2006 1.1.-31.3.
Cash flows from operating activities:			
Loss for the period		(1.229)	(588)
Adjustments for:			
Depreciation		752	867
Other operating items	6	(1.774)	(699)
Working capital used in operations		(2.251)	(420)
Net change in operating assets and liabilities		2.937	1.399
Net cash from operating activities		686	979
Cash flows from investing activities:			
Acquisition of operating assets		(2.650)	(1.851)
Proceeds from the sale of operating assets		225	1.746
Acquisition of intangible assets		(1)	(41)
Acquisition of subsidiaries, net of cash acquired		0	5.023
Long-term receivables, increase		(200)	(43)
Current receivables, change		0	(1.462)
Net cash (used in) from investing activities		(2.626)	3.372
Cash flows from financing activities:			
Acquisition of own shares		(308)	0
Proceeds from long term borrowings		7.723	0
Repayment of long term borrowings		(7.444)	(786)
Proceeds from short term borrowings		468	0
Net cash from (used in) financing activities		439	(786)
(Decrease) increase in cash and cash equivalents		(1.501)	3.565
Effect of exchange rate fluctuations on cash held		(42)	65
Cash and cash equivalents at 1 January		2.776	0
Cash and cash equivalents at 31 March		1.233	3.630
Investment and financing without cash flow effect:			
Receivables from sale of operating assets	3	11.665	0

Interim Financial Statements of Icelandair Group hf. 31 March 2007 Amounts are in ISK million

Notes

Significant accounting policies

Icelandair Group hf. ("the Company") is a limited liability company incorporated and domiciled in Iceland. The address of the Company´s registered office is at Reykjavíkurflugvöllur in Reykjavík, Iceland. The consolidated interim financial statements of the Company as at and for the three-month period ended 31 March 2007 comprise the Company and its subsidiaries (together referred to as the "Group") and the Group´s interests in associates. The Group´s operations are in the airline transportation and tourism industry. The interim financial statements were authorised for issue by the board of directors on 15 May 2007.

a. ***Statement of compliance***

These condensed consolidated interim financial statements have been prepared in accordance with International Financial Reporting Standard IAS 34, Interim Financial Reporting. They do not include all of the information required for a complete set of consolidated annual financial statements, and should be read in conjunction with the consolidated financial statements of the Company as at and for the year ended 31 December 2006.

b. ***Basis of preparation***

The accounting policies and methods of computation applied by the Company in these condensed interim consolidated financial statements are the same as those applied by the Company in its consolidated financial statements as at and for the year ended 31 December 2006. The consolidated financial statements for the year ended 31 December 2006 are available at the Company's office and website, www.icelandairgroup.is and at The Icelandic Stock Exchange website, www.omxgroup.is.

The condensed consolidated interim financial statements are prepared in Icelandic kronas, which is the Company's functional currency, rounded to the nearest million. They are prepared on the historical cost basis except that derivative financial instruments are stated at their fair value.

c. ***Pro forma information***

Compiled pro forma figures for the first three months of the year 2006 are presented in the income statement and statement of cash flows. The pro forma figures consist of the consolidated interim income statement and statement of cash flows of the Group for the the first three months of the year 2006, as if the acquisition of Icelandair Group hf. had been effected at the beginning of the year 2006. For this purpose, the consolidated interim pro forma income statement and statement of cash flows of the Group for the first three months of the year 2006 have been prepared in accordance with the accounting policies disclosed in these consolidated interim financial statements and are based on the compiled financial statements of all subsidiaries of Icelandair Group hf. for the first three months of the year 2006.

d. ***Equity settled share-based payment transactions***

The Company issued share options to employees at the beginning of the year and adopted IFRS 2, Share-based Payment.

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

Notes, cont.:

d. Contd.:

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

The Company has granted options for 60.3 million shares at the excercise price 27.5. The options vest in 12 to 36 months.

Segment reporting

1. Business segments for the period from 1 January to 31 March 2007:

	Scheduled airline operations	Global capacity and aircraft trading	Travel and tourism infrastructure	Shared services	Eliminations	Consolidated
Segment revenue	10.228	3.198	1.521	164	(3.206)	11.905
Segment EBITDA	(812)	909	2	(180)		(81)
Segment results	(1.213)	814	(120)	(314)		(833)
Net finance costs	(199)	(95)	(12)	(463)		(769)
Share of profit of .... associates	0	61	0	0		61
Income tax	253	(117)	24	152		312
(Loss) profit for the period .	(1.159)	663	(108)	(625)		(1.229)
Segment assets	30.015	25.346	5.198	45.270	(32.368)	73.461
Investments in .... associates	2	2.206	4	0		2.212
Total assets	30.017	27.552	5.202	45.270	(32.368)	75.673
Segment liabilities	25.743	24.781	4.265	20.557	(23.724)	51.622
Capital expenditure	1.336	1.132	179	3		2.650
Depreciation	366	95	108	2		571
Amortisation of .... intangible assets	73	88	18	2		181

Interim Financial Statements of Icelandair Group hf. 31 March 2007 Amounts are in ISK million

Finance income and finance expense

2. Finance income and finance expense are specified as follows:

	2007 1.1.-31.3.	Pro forma 2006 1.1.-31.3.
Interest income on bank deposits	27	131
Other interest income	19	44
Net foreign exchange gain	0	596
Finance income total	46	771
Interest expense on loans and borrowings	687	355
Other interest expenses	13	10
Net foreign exchange loss	115	0
Finance expense total	815	365
Net finance (costs) income	(769)	406

Receivables from sale of aircrafts

3. At year end 2006 the Group had made prepayments on six Boeing 737-800 aircrafts to be delivered in 2007. During the first quarter of 2007 the Group sold all these aircrafts. The Group also sold three other aircrafts during the quarter, two of them on a sale and leaseback contracts to 5 and 6 years. Those two aircrafts were purchased during the first quarter.

Total capital gain on sale amounted to ISK 1,196 million. Receivables from sale of aircraft amounted to ISK 11,665 million which will be paid during the year.

Equity

4. The Company's share capital amounts to ISK 1,000 million as decided in its Articles of Association. The holders of ordinary shares are entitled to receive dividends as declared from time to time and are entitled to one vote per share of one ISK.

Share premium

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

Share option reserve

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

Hedging reserve

The hedging reserve 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.

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4. Contd.:

Translation reserve

The translation reserve comprises all foreign currency differences arising from the translation of the financial statements of foreign operations as well as from the translation of liabilities that hedge net investment in a foreign subsidiary.

Group entities

5. The Company holds twelve subsidiaries at the end of the quarter, but they were forteen at year end 2006. On 1 January 2007, Icelandair Technical Services ehf. merged into Icelandair ehf. and Blue Cargo ehf. merged into Bluebird Cargo ehf. The subsidiaries, which are all included in the consolidated interim financial statements, are:

	Share
Scheduled airline operations:	
Icelandair ehf.	100%
Icelandair Cargo ehf.	100%
Icelandair Ground Services ehf. (IGS)	100%
Global capacity solutions and aircraft trading:	
Bluebird Cargo ehf.	100%
IceLease ehf.	100%
IG Invest ehf.	100%
Loftleiðir - Icelandic ehf.	100%
Travel and tourism infrastructure:	
Air Iceland ehf.	100%
Iceland Travel ehf.	100%
Icelandair Hotels ehf.	100%
Shared services:	
IceCap Ltd., Guernsey	100%
Icelandair Shared Services ehf.	100%

The subsidiaries own 18 subsidiaries that are all included in the consolidated interim financial statements.

Statement of cash flows

6. Other operating items in the statement of cash flows are specified as follows:

	2007 1.1.-31.3.	**Pro forma** 2006 1.1.-31.3.
Gain on the sale of assets	(1.196)	(432)
Exchange rate difference and indexation of liabilities and assets	(205)	(129)
Share of profit of associates	(61)	(9)
Income tax expense	(312)	(129)
Total other operating items in the statement of cash flows	(1.774)	(699)

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Ratios

7. The Group's primary ratios are specified as follows:

	31.3.2007	31.12.2006
Working capital ratio	0,62	0,40
Equity ratio	0,32	0,34
Intrinsic value of share capital	24,32	26,00