

Icelandair Group hf.
Condensed Consolidated
Interim Financial Statements
1 January - 31 March 2014

USD

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

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Endorsement and Statement by 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 2014 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. (the "Company") and its subsidiaries together referred to as the "Group". The condensed consolidated Interim financial statements are stated in thousands of USD.

According to the consolidated statement of comprehensive income, loss for the period from 1 January to 31 March amounted to USD 26.7 million. Total comprehensive loss for the period was USD 28.3 million. According to the consolidated statement of financial position, equity at the end of the period amounted to USD 298.7 million, including share capital in the amount of USD 40.6 million. Reference is made to the notes to the consolidated statement of changes in equity regarding information on changes in equity.

Statement by the Board of Directors and the CEO

The condensed consolidated interim financial statements for the three months ended 31 March 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. The condensed consolidated interim financial statements have not been audited or reviewed by the Company's independent auditors.

According to our best knowledge it is our opinion that the condensed consolidated interim financial statements give a true and fair view of the financial performance of the Group for the three month period ended 31 March 2014, its assets, liabilities and consolidated financial position as at 31 March 2014 and its consolidated cash flows for the period then ended.

Further, in our opinion the condensed consolidated interim 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 condensed consolidated interim financial statements of Icelandair Group hf. for the period from 1 January to 31 March and confirm them by means of their signatures.

Reykjavík, 30 April 2014.

Board of Directors:

Sigurður Helgason, Chairman of the Board
Úlfar Steindórsson
Ásthildur M. Otharsdóttir
Elín Jónsdóttir
Katrín Olga Jóhannesdóttir
Magnús Magnússon

CEO:

Björgólfur Jóhannsson

Consolidated Statement of Comprehensive Income for the period from 1 January to 31 March 2014

	Notes	2014 1.1.-31.3.	2013 1.1.-31.3.
Operating income			
Transport revenue	6	121.580	110.067
Aircraft and aircrew lease		21.961	28.352
Other operating revenue	6	47.736	34.626
		191.277	173.045
Operating expenses			
Salaries and other personnel expenses	7	60.889	52.280
Aircraft fuel		47.971	43.596
Aircraft lease		6.007	9.638
Aircraft handling, landing and communication		14.372	12.676
Aircraft maintenance expenses		21.067	18.403
Other operating expenses	7	54.275	44.766
		204.581	181.359
Operating loss before depreciation and amortisation (EBITDA)		(13.304)	(8.314)
Depreciation and amortisation		(17.296)	(14.684)
Operating loss before net finance (costs) income (EBIT)		(30.600)	(22.998)
Finance income		460	2.550
Finance costs		(3.147)	(2.521)
Net finance (costs) income	8	(2.687)	29
Share of (loss) profit of associates, net of tax		(75)	46
Loss before tax		(33.362)	(22.923)
Income tax		6.641	4.634
Loss for the period		(26.721)	(18.289)
Other comprehensive loss:			
Currency translation differences		752	1.066
Net profit on hedge of investment, net of tax		47	87
Effective portion of changes in fair value of cash flow hedge, net of tax		(2.347)	396
Other comprehensive (loss) profit for the period		(1.548)	1.549
Total comprehensive loss for the period		(28.269)	(16.740)

The notes on pages 9 to 15 are an integral part of these interim consolidation financial statements.

Consolidated Statement of Comprehensive Income for the period from 1 January to 31 March, contd.:

	2014	2013
	1.1.-31.3	1.1.-31.3
Loss attributable to:		
Owners of the Company	(26.721)	(18.264)
Non-controlling interest	0	(25)
Loss for the period	<u>(26.721)</u>	<u>(18.289)</u>
Total comprehensive loss attributable to:		
Owners of the Company	(28.269)	(16.651)
Non-controlling interest	5	(89)
Total comprehensive loss for the period	<u>(28.264)</u>	<u>(16.740)</u>
Earnings per share:		
Basic loss per share expressed in USD cent per share	(0,54)	(0,37)
Diluted loss per share expressed in USD cent per share	(0,54)	(0,37)

The notes on pages 9 to 15 are an integral part of these interim consolidation financial statements.

Consolidated Statement of Financial Position as at 31 March 2014

	Notes	31.3.2014	31.12.2013
Assets			
Operating assets	9	310.947	299.197
Intangible assets and goodwill		179.741	179.676
Investments in associates		2.764	2.035
Long-term cost		248	258
Non-current receivables and deposits		16.851	15.791
Non-current assets		510.551	496.957
Inventories		23.516	22.166
Trade and other receivables		133.470	114.259
Marketable securities		9.541	7.955
Cash and cash equivalents		250.213	191.538
Current assets		416.740	335.918
Total assets		927.291	832.875
Equity			
Share capital		40.576	40.576
Share premium		154.705	154.705
Reserves	10	30.153	31.706
Retained earnings		73.044	118.856
Equity attributable to equity holders of the Company		298.478	345.843
Non-controlling interest		244	239
Total equity		298.722	346.082
Liabilities			
Loans and borrowings	11	74.600	78.489
Other payables		18.075	23.742
Deferred tax liabilities		21.273	27.995
Non-current liabilities		113.948	130.226
Loans and borrowings	11	19.127	43.528
Trade and other payables		204.965	159.504
Deferred income		290.529	153.535
Current liabilities		514.621	356.567
Total liabilities		628.569	486.793
Total equity and liabilities		927.291	832.875

The notes on pages 9 to 15 are an integral part of these interim consolidation financial statements.

Consolidated Statement of Changes in Equity for the period from 1 January to 31 March 2014

Attributable to equity holders of the Company							
	Share capital	Share premium	Reserves	Retained earnings	Total	Non-con- trolling interest	Total equity
1 January to 31 March 2013							
Equity 1.1.2013	40.576	154.705	26.164	74.230	295.675	257	295.932
Total comprehensive loss			1.549	(18.264)	(16.715)	(89)	(16.804)
Dividend (0.24 USD cent per share) ...				(11.820)	(11.820)		(11.820)
Equity 31.3.2013	40.576	154.705	27.713	44.146	267.140	168	267.308
1 January to 31 March 2014							
Equity 1.1.2014	40.576	154.705	31.706	118.856	345.843	239	346.082
Total comprehensive loss			(1.548)	(26.721)	(28.269)	5	(28.264)
Dividend (0.38 USD cent per share) ...				(19.091)	(19.091)		(19.091)
Equity 31.3.2014	40.576	154.705	30.158	73.044	298.483	244	298.727

Information on changes in reserves are provided in note 11.

The notes on pages 9 to 15 are an integral part of these interim consolidation financial statements.

Consolidated Statement of Cash Flows for the three months ended 31 March 2014

	Notes	2014 1.1.-31.3.	2013 1.1.-31.3.
Cash flows from operating activities			
Loss for the period		(26.721)	(18.289)
Adjustments for:			
Depreciation and amortisation		17.296	14.684
Other operating items	17	(3.124)	2.124
Working capital to operations		(12.549)	(1.481)
Net change in operating assets and liabilities	18	133.920	79.934
Net cash from operating activities		121.371	78.453
Cash flows used in investing activities:			
Acquisition of operating assets		(27.413)	(41.031)
Proceeds from the sale of operating assets		232	175
Acquisition of intangible assets		(530)	(529)
Long-term cost, change		(2.995)	(1.542)
Long-term receivables, change		(1.654)	(1.111)
Marketable securities, change		(1.586)	3.243
Net cash used in investing activities		(33.946)	(40.795)
Cash flows used in financing activities:			
Repayment of long term borrowings		(29.138)	(11.239)
Net cash used in financing activities		(29.138)	(11.239)
(Decrease) increase in cash and cash equivalents		58.287	26.419
Effect of exchange rate fluctuations on cash held		388	479
Cash and cash equivalents at beginning of the period		191.538	117.060
Cash and cash equivalents at 31 March		250.213	143.958
Investment and financing without cash flow effect:			
Dividend issued		(19.091)	(11.820)
Trade and other payables		19.091	11.820

Information on interest paid and received are provided in note 20.

The notes on pages 9 to 15 are an integral part of these interim consolidation financial statements.

Notes

1. Reporting entity

Icelandair Group hf. (the "Company") is a public limited liability company incorporated and domiciled in Iceland. The condensed consolidated interim financial statements of the Company as at and for the three months ended 31 March 2014 comprise the Company and its subsidiaries (together referred to as the "Group") and the Group's interests in associates. The Group is primarily involved operates in the airline transportation and tourism industry. The Company is listed on the Nasdaq OMX Iceland.

The Group's consolidated financial statements as at and for the year ended 31 December 2013 are available upon request from the Company's registered office at Reykjavíkurlugvöllur in Reykjavík, Iceland or at its website address, www.icelandairgroup.is and at The Icelandic Stock Exchange website, www.nasdaqomx.com.

2. Basis of preparation

a. Statement of compliance

The condensed consolidated interim financial statements have been prepared in accordance with International Financial Reporting Standard IAS 34, *Interim Financial Reporting*. Selected explanatory notes are included to explain events and transactions that are significant to an understanding of the changes in financial position and performance of the Group since the last annual consolidated financial statements as at and for the year ended 31 December 2013. These condensed consolidated interim financial statements do not include all the information required for full annual financial statements prepared in accordance with International Financial Reporting Standards.

These condensed consolidated interim financial statements were approved for issue by the Board of Directors on 30 April 2014.

Except as described below the accounting policies and methods of computation applied by the Group in these condensed interim consolidated financial statements are the same as those applied by the Group in its consolidated financial statements as at and for the year ended 31 December 2013.

b. Restatement of comparative figures

When preparing the financial statements, new and improved methods of eliminating intercompany transactions were put in place. As the change affects the classification of cost, comparative figures for 2013 have been adjusted accordingly. The effect on the comparative figures is a reduction in Aircraft and aircrew lease of USD 7 million and comparative increase in Aircraft maintenance expenses. Insignificant adjustments were made to other line items of operating expenses. The restatement of the comparative amounts has no other effect on the consolidated financial statements.

3. Significant accounting policies

Functional and presentation currency

These condensed Consolidated Interim Financial Statements are presented in U.S. dollars (USD), which is the Company's functional currency. All financial information presented in USD has been rounded to the nearest thousand, except when otherwise indicated.

Notes, contd.:

3. *Continued:*

The Group has adopted all new standards and amendments to standards with a date of initial application of 1 January 2013 that have been approved by the EU. Of those standards only IFRS 13, *Fair Value Measurements and changes to IAS 34 as part on annual improvements 2009-2011 cycle* had effects on these condensed interim financial statements.

IFRS 13 establishes a single framework for measuring fair value and making disclosures about fair value measurements, when such measurements are required or permitted by other IFRSs. In particular, it unifies the definition of fair value as the price at which an orderly transaction to sell an asset or to transfer a liability would take place between market participants at the measurement date. It also replaces and expands the disclosure requirements about fair value measurements in other IFRSs, including IFRS 7 *financial Instruments: Disclosures*. Some of the disclosures are specifically required in interim financial statements for financial instruments; accordingly, the Group has included additional disclosures in this regard.

In accordance with the transitional provisions of IFRS 13, the Group has applied the new fair value measurement guidance prospectively, and has not provided any comparative information for disclosures that were not previously required. Notwithstanding the above the change had no significant impact on the measurement of the Group's assets and liabilities.

4. **Judgements and estimates**

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

In preparing these condensed consolidated interim financial statements, the significant judgements made by management in applying the Group's accounting policies and the key sources of estimation uncertainty were the same as those that applied to the consolidated financial statements as at and for the year ended 31 December 2013.

Notes, contd.:

5. Operating segment

Segment information is presented in the interim 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.

Route network

Seven companies are categorised as part of the Route Network: Icelandair, Icelandair Cargo, Loftleidir, Air Iceland, Icelandair Ground Services, FERIA ehf. and FjÁrvakur - Icelandair Shared Services.

Tourism services

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

Reportable segments for the three months ended 31 March 2014

	Route network		Tourism services		Total	
	2014	2013	2014	2013	2014	2013
External revenue	175.573	159.978	15.612	12.304	191.185	172.282
Inter-segment revenue	32.874	35.745	368	521	33.242	36.266
Segment revenue	<u>208.447</u>	<u>195.723</u>	<u>15.980</u>	<u>12.825</u>	<u>224.427</u>	<u>208.548</u>
Segment EBITDAR*	(729)	5.948	(921)	(714)	(1.650)	5.234
Segment EBITDA	(8.502)	(4.392)	(3.315)	(2.810)	(11.817)	(7.202)
Loss before taxes	(27.063)	(17.634)	(4.142)	(3.268)	(31.205)	(20.902)
Segment assets	<u>721.414</u>	<u>694.855</u>	<u>29.513</u>	<u>25.408</u>	<u>750.927</u>	<u>720.263</u>

Reconciliation of reportable segment income

	2014	2013
	1.1.-31.3.	1.1.-31.3.
Total loss for reportable segments	(31.205)	(20.902)
Unallocated amounts:		
Other corporate expenses	(2.082)	(2.067)
Share of (loss) profit of equity accounted investees	(75)	46
Consolidated loss before income tax	<u>(33.362)</u>	<u>(22.923)</u>

Other material items 31 March 2014

	Reportable segment	Adjustments	Consolidated
Segment EBITDAR*	(1.650)	(1.487)	(3.137)
Segment EBITDA	(11.817)	(1.487)	(13.304)

* EBITDAR means EBITDA before operating lease expenses.

Seasonality

The Group's business is highly seasonal with highest demand during the summer months.

Notes, contd.:

6. Operating income

Transport revenue is specified as follows:

	2014	2013
	1.1.-31.3.	1.1.-31.3.
Passengers	110.392	99.976
Cargo and mail	11.188	10.091
Total transport revenue	<u>121.580</u>	<u>110.067</u>

Other operating revenue is specified as follows:

Sale at airports and hotels	9.225	7.827
Revenue from tourism	13.303	11.727
Aircraft and cargo handling services	8.132	7.413
Maintenance revenue	9.141	1.289
Gain on sale of operating assets	69	61
Other operating revenue	7.866	6.309
Total other operating revenue	<u>47.736</u>	<u>34.626</u>

7. Operating expenses

Salaries and other personnel expenses are specified as follows:

Salaries	37.966	32.211
Salary-related expenses	12.107	10.749
Other personnel expenses	10.816	9.320
Total salaries and personnel expenses	<u>60.889</u>	<u>52.280</u>

Other operating expenses are specified as follows:

Operating cost of real estate and fixtures	5.569	4.700
Communication	4.422	3.504
Advertising	5.812	5.267
Booking fees and commission expenses	12.256	9.387
Cost of goods sold	4.427	3.921
Customer services	3.574	2.230
Tourism expenses	7.151	6.136
Allowance for bad debt	3.834	2.115
Other operating expenses	7.230	7.506
Total other operating expenses	<u>54.275</u>	<u>44.766</u>

Notes, contd.:

8. Finance income and finance costs

Finance income and finance costs are specified as follows:

	2014 1.1.-31.3.	2013 1.1.-31.3.
Interest income on bank deposits	330	157
Other interest income	130	541
Net foreign exchange gain	0	1.852
Finance income total	460	2.550
Interest expenses on loans and borrowings	1.735	2.195
Other interest expenses	163	326
Net foreign exchange loss	1.249	0
Finance costs total	3.147	2.521
Net finance (costs) income	(2.687)	29

9. Operating assets

Aquisition of operating assets in the first three months of 2014 amounted to USD 27.4 million. Included is one Boeing 757 aircraft and overhaul of own engines of USD 18.3 million.

10. Equity

Reserves are specified as follows:

	Hedging reserve	Translation reserve	Total reserves
Reserves 1.1.2013	(1.338)	27.502	26.164
Changes during the period	396	1.153	1.549
Reserves 31.3.2013	(942)	28.655	27.713
Reserves 1.1.2014	(108)	31.814	31.706
Changes during the period	(2.347)	799	(1.548)
Reserves 31.3.2014	(2.455)	32.613	30.158

11. 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.

	31.3.2014	31.12.2013
Non-current loans and borrowings are specified as follows:		
Secured bank loans	80.083	107.621
Unsecured loans	13.644	14.396
	93.727	122.017
Current maturities	(19.127)	(43.528)
Total non-current loans and borrowings	74.600	78.489

Terms and debt repayment schedule:

	Currency	Nominal interest rates	Year of maturity	Total remaining balance	
				31.3.2014	31.12.2013
Secured bank loan	USD	5,2%	2014-2018	47.862	74.921
Secured bank loan	EUR	3,7%	2017	15.095	15.518
Secured bank loan	ISK	7,3%	2017-2023	16.127	16.209
Secured bank loan, indexed	ISK	6,3%	2021-2028	999	973
Unsecured bond issue, indexed	ISK	5,7%	2023	13.644	14.396
Total interest-bearing liabilities				93.727	122.017

Notes, contd.:

12. Contractual repayments of loans and borrowings

Repayments of loans and borrowings are specified as follows:

	2014	2013
Repayments in 2014 (9 months)(2013: 12 months)	14.534	43.528
Repayments in 2015	15.985	15.898
Repayments in 2016	16.439	16.350
Repayments in 2017	29.710	29.471
Repayments in 2018	7.472	7.430
Subsequent repayments	9.587	9.340
Total loans and borrowings	93.727	122.017

13. Financial instruments and fair values

The fair values of financial assets and liabilities, together with the carrying amounts shown in the statement of financial position, are as follows:

	31.3.2014		31.12.2013	
	Carrying amount	Fair value	Carrying amount	Fair value
Derivatives, included in loans and receivables	0	0	1.853	1.853
Marketable securities	9.541	9.541	7.955	7.955
Unsecured bond issue	(13.644)	(15.622)	(14.396)	(17.398)
Secured bond loans	(80.083)	(88.433)	(107.621)	(117.219)
Derivatives, included in payables and prepayments	(2.677)	(2.677)	(2.050)	(2.050)
Total	(86.863)	(97.191)	(114.259)	(126.859)

14. Off-balance sheet items

As a lessee the Group has in place operating leases for 10 aircraft at the end of March 2014. The leases are for 5 Boeing 757 aircraft, 2 Boeing 767 aircraft and 3 Boeing 737 aircraft. The Group also has in place operating leases for storage facilities, accommodations, equipment and fixtures for its operations, the longest until the year 2039. At the end of March 2014 the leases are payable as follows in nominal amounts for each year:

				Total
	Real estate	Aircraft	Other	31.3.2014
In Q2 - Q4 2014	10.686	18.535	2.568	31.789
In the year 2015	14.962	22.293	1.492	38.746
In the year 2016	16.123	16.443	798	33.364
In the year 2017	14.869	13.113	739	28.721
In the year 2018	14.780	11.185	0	25.965
Subsequent	176.776	10.575	0	187.351
Total	248.195	92.144	5.596	345.936

15. 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 is valued at USD 1.6 billion at Boeing list prices. 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 acquisition will be funded by internal resources and from aviation finance products.

Notes, contd.:

16. Group entities

The Company held eleven subsidiaries at the end of March 2014. The subsidiaries included in the consolidated interim financial statements are as follows:

	Share
Route network:	
Air Iceland ehf.	100%
Feria ehf.	100%
Fjárvakur - Icelandair Shared Services ehf.	100%
Icelandair ehf.	100%
Icelandair Cargo ehf.	100%
IGS ehf.	100%
Lofleiðir - Icelandic ehf.	100%
Tourism services:	
Iceland Travel ehf.	100%
Icelandair Hotels ehf.	100%
Other operations:	
A320 ehf.	100%
IceCap Ltd., Guernsey	100%

The subsidiaries further own 17 subsidiaries that are all included in the consolidated interim financial statements.

17. Statement of cash flows

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

	2014 1.1.-31.3.	2013 1.1.-31.3.
Expensed long-term cost	3.079	6.371
Exchange rate differences	431	494
Gain on sale of operating assets	(69)	(61)
Share in loss (profit) of associates	75	(46)
Income tax	(6.640)	(4.634)
Other operating items total	(3.124)	2.124

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

Inventories, increase	(1.350)	(2.771)
Trade and other receivables, increase	(22.863)	(18.956)
Trade and other payables, increase	21.484	7.800
Deferred income, increase	136.649	93.861
Net change in operating assets and liabilities	133.920	79.934

19. Additional cash flow information:

Interest expenses paid	3.022	3.415
Interest income received	208	683

20. Ratios

The Group's primary ratios are specified as follows:

	31.3.2014	31.12.2013
Current ratio	0,81	0,94
Equity ratio	0,32	0,42
Intrinsic value of share capital	7,36	8,53