

Iceland



Icelandair's 2009 full-year results revealed that revenues increased by 11% to €472.3m, while costs, including fuel, fell but aircraft leasing cost increased by 43%.

MARKET REVIEW

Air traffic agreements. In recent years there has been a significant increase in the number of bilateral air transport agreements between Iceland and other states. As a result of its participation in the annual ICAO Conference for Air Service Negotiations (ICAN) in Istanbul in 2009, Iceland signed new bilateral air transport agreements with Vietnam, Kuwait, Azerbaijan, Turkmenistan, Syria and the Dominican Republic.

The Icelandic government is hoping to reap further benefits from its participation in the ICAN of 2010 hosted in Jamaica from June 27 to July 2.

Effective as of the beginning of 2010, the EU-US Open Skies Air Transport Agreement has now been made applicable to Iceland and Norway following the decision of the EU Council of Ministers.

Further, negotiations are ongoing on Iceland becoming a party to all Comprehensive Air Services Agreements between the EU and its member states on the one part and third states on the other part.

Work is in progress on amendments to the constitutive agreement of the EFTA organisation, the Agreement forming the European Economic Area and the EU-Switzerland bilateral agreement in order to secure traffic rights from the member states of the EU and EFTA to Switzerland and *vice versa*.

Commercial aviation. On April 14, 2010 Iceland notoriously became the centre of not so welcome international attention when the sub-glacier volcano with the tongue-twisting name of *Eyjafjallajökull* erupted after almost two centuries of no activity.

The airline industry, so accustomed to the uninterrupted access to the air, was abruptly reminded that at the end of the day it stands to the whim of the forces of Mother Nature.

Commercial aviation, already struggling to recover from the economic crisis, was seriously hit by the *Eyjafjallajökull* volcanic eruption. The explosive eruption led to a massive closure of airspace in Europe for six days, and temporary closures in different parts of Europe's airspace afterwards, causing over 100,000 flights to be cancelled.

The response to the ash plume's

Leasing Companies

Avion Aircraft Trading ehf

Grófin 1, 101 Reykjavik, Iceland. Tel: +354 515 7700; Fax: +354 515 7799; Email aat@aat.is; Website: www.aat.is. Director: Magnus G. Thorstenn; Tel: +354 897 0320; Email: magnus@aat.is.

Activities: Aircraft trading lease management consulting portfolio mainly widebody freighters B747-400 with over 26 OEM and converted freighters.

Legal Consultants/ Accountants

Logos Legal Services

Efstaleiti 5, IS-103 Reykjavik, Iceland. Tel: +354 540 0300; Fax: +354 540 0301; Email: logos@logos.is; Website: www.logos.is. Managing Partner: Gunnar Sturluson; Email: gunnar@logos.is; Partner: Erlendur Gislason; Email: erlendur@logos.is.

Activities: Advice to lessees, lessors and financiers on aircraft leasing and financing. Aircraft registrations and mortgage filing and related activities in Iceland and Denmark.

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arrival in the UK and adjacent air space was predominantly reactive and therefore less effective than it could have been. This was, in part, a result of the failure to recognise in advance the potential threat presented by volcanic ash clouds from Iceland.

The situation was made worse by inflexible aviation protocols and by the absence of any pre-existing agreement on safe ash levels. This resulted in too far-reaching and lengthy closures of air-space.

Airlines in some countries have addressed the issue of state liability to airlines for their losses caused by the stringent application of aviation protocols. So far, no such claims have been raised by the Icelandic airlines *vis-à-vis* the Icelandic state or other states.

Air traffic is highly likely to be disrupted by future eruptions at volcanoes in Iceland or elsewhere in the region. Consequently there is a serious need to be better prepared in order to minimise the impact.

It is to be hoped that there will be improvements and better overall prepa-

ration through the IATA and ICAO shared initiative in April 2010 to create a task force that will expedite research to agree on specific technical standards for engine tolerance to volcanic ash.

Following the eruption it has been the airlines' common view that the EU rules for compensation and passenger welfare for flight irregularities placed an unfair burden on airlines.

It cannot be denied that there is a contradiction in an airline having to pick up a passenger welfare cost of hundreds or thousands of euros for a stranded passenger whose ticket was purchased at a fraction of the cost of the passenger care and welfare.

It is food for thought why the *force majeure* defence is only available to airlines as a defence with respect to compensation claims, while EU Regulation 261/2004 stipulates that the defence cannot be invoked with respect to passenger care. Following this costly lesson, a rethinking of the EU flights cancellation compensation system is required.

Scheduled air services. *Icelandair*. In the wake of the Icelandic banking crisis at

the end of 2008 and during 2009, the previous majority owners of Icelandair saw their shares acquired by the new banks, now owned by the state and foreign creditors of the failed banks.

With the financial restructuring of the airline drawing to a completion, new share capital is being issued in 2010 and has been sold to one of the largest Icelandic pension funds and to a new entrepreneurial fund (*Framtakssjóður*) set up by Icelandic pension funds in order to stimulate core businesses vital for the local economy.

Steps are also being taken to broaden still further the shareholder group of the flag carrier, with a share offering to qualified investors as well as a public offering expected to take place later in 2010. All these new share issues are expected to improve the carrier's liquidity and strengthen its balance sheet.

As part of its financial restructuring, Icelandair Group, the airline, travel and tourism group of companies, will be divesting certain non-core operating subsidiaries such as Czech airline Travel Service (20% stake left), Latvian

LOGOS

LEGAL SERVICES
SINCE 1907

CONTACT:

Erlendur Gislason
erlendur@logos.is

Efstaleiti 5
103 Reykjavík
+ 354 5 400 300
+ 354 5 400 301
logos@logos.is

42 New Broad Street
London EC2M 1JD
+ 44 (0) 207 920 3020
+ 44 (0) 207 920 3099
logos@logos.is

Lautrupsgade 7, 4th floor
DK-2100 Copenhagen
Tel. + 45 70 229 224
Fax + 45 70 274 279
logoslaw@logos.dk

COMPANY PROFILE:

LOGOS is a limited partnership focusing on providing high quality legal services to both domestic and international businesses. Many of the largest corporations in Iceland, both listed and non-listed, are among LOGOS' clients and LOGOS provides extensive services to international entities.

LOGOS has a long experience in advising banks and financial institutions on aircraft financing and security related issues, as well as lessors placing aircraft on lease into and out of the Icelandic market. Among its clients is Icelandair, the flag carrier of Iceland.

Among its other airline clients are the Primera Travel Group and Air Atlanta Icelandic, both active players in the charter and ACMI services market.

LOGOS has offices in Reykjavik, London and Copenhagen. Clients benefit from the firm's international resources in structuring and advising on transactions.

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In 2009 Air Atlanta Icelandic added four Boeing B747-400 aircraft which marks a turning point in its fleet development.

SmartLynx Airlines and Bluebird Cargo.

Notwithstanding problems at the shareholder level, the airline operation shows healthy signs and the group will be heading back to basics, giving priority to Iceland-centred travel and tourism around its Keflavik hub as before the post-2004 expansion into foreign investment.

Icelandair continues to operate an all Boeing B757 and B767 fleet of aircraft, using only the narrowbody in its scheduled operations, while the airline's three B767s form a part of the capacity solutions operations of the Loftleidir Icelandic subsidiary. The B757 aircraft has served the airline well with respect to capacity and range.

However, with no new production, the fleet is inevitably aging, the oldest manufactured as early as 1990. Thus, the airline is now looking at replacements in the not so distant future. A likely candidate is thought to be next generation B737s, although no decision has been taken yet.

Iceland Express. Iceland Express remains the second Icelandic scheduled airline operating on a number of routes in Scandinavia, UK and continental Europe. The airline's flights are operated by UK operator Astraesus.

Iceland Express started trans-Atlantic flights to New York's Newark airport on June 8, 2010, thus starting the first ever competition between two Icelandic entities on the Iceland-US route.

Iceland's inclusion in the EU-US Open Skies Agreement is making Iceland Express's entry into this route possible as its flights are operated by UK carrier Astraesus.

ACMI and charter operations. *Air Atlanta Icelandic.* While Icelandair is the main scheduled airline in Iceland, Air Atlanta Icelandic remains the leading ACMI provider operating out of Iceland.

After an unsuccessful merger with Íslandsflug in 2005, which resulted in an airline with a disadvantageous fleet of 46 aircraft of 10 different types, in 2006 and 2007 the airline started to downsize to its current fleet of 20 widebody aircraft, nine of which are passenger and 11 cargo aircraft.

In 2009 Air Atlanta Icelandic added four Boeing B747-400 aircraft which marks a turning-point in its fleet development. Air Atlanta's main customers are airlines in Europe, Middle East and Asia.

The recent downsizing exercise has proven costly, but with cost cutting, financial reconstruction and modernisation of its fleet, the airline's management believes it is prepared for the challenges ahead and is expecting to get out of "the red" later in 2010.

The local charter market is still to recover from the sharp decline since the start of the recession at the end of 2008.

Primera Air. Primera Air, a part of the Primera Travel Group operating in Iceland and Scandinavia, finished the migration of its fleet of aircraft out of Iceland and onto the Danish aircraft registry in 2009 and now all its six aircraft are registered in Denmark where the Danish subsidiary Primera Air Scandinavia ApS is issued with an Air Operator's Certificate.

The airline has now returned all its MD-82/3 aircraft and will now be operating next generation B737 aircraft only,

with five Boeing B737-800s and one B737-700 comprising its fleet. With one new aircraft delivery planned for each of 2011 and 2012, the airline plans to be operating a fleet of 12 aircraft in 2014.

Around 80% of the airline operation is servicing the Primera Travel Group tour operators, the two main hubs being Arlanda and Billund, whereas it no longer operates out of Ireland following the bankruptcy of the Irish tour operator belonging to the group.

Cargo operations. *Icelandair Cargo.* The main cargo carrier in Iceland, Icelandair Cargo, made a strategic change in 2008, emphasising its core operations in its Icelandic home market rather than the North Atlantic in general. This has proved successful and the company considers its prospects as positive.

Exports are going fine and imports are rising again after a sharp reduction at the end of 2008 and through 2009.

The cargo airline, operating under the Icelandair certificate, operates five Boeing B757-200 aircraft, one to two dedicated to the scheduled operations to and from Iceland, depending on demand, and three to four doing ACMI services for TNT.

Bluebird Cargo. After having been a wholly owned subsidiary of Icelandair Group since 2005, Bluebird Cargo is now one of the subsidiaries considered by Icelandair Group and its financiers to be a non-core operation and which the group intends to sell in the near future.

The carrier operates a fleet of five Boeing B737-300/400s, one owned by the carrier and four on lease. One aircraft is servicing the Icelandic market which connects to the route network of Cargolux, while four are leased out on an ACMI basis.

One more year has passed and still the outlook for commercial aviation is not too bright. As if high oil prices, the credit crunch, bank collapse and overall financial crisis were not disruptive enough, natural catastrophes added to the never-ending adversities facing aviation.

Eyjafjallajökull has gone quiet for now and the neighbouring volcano *Katla* shows no sign of erupting. It is hoped that both the economy and nature will treat aviation more gently in the coming months and years than we have experienced of late.

This article was written by Erlendur Gíslason, Partner, LOGOS legal services, Efstaleiti 5, IS-103 Reykjavík, Iceland. Tel: +354 5400 300. Fax: +354 5400 301. Email: erlendur@logos.is. Website: www.logos.is.