

DONEGAL GROUP INC.

AGENCY STOCK PURCHASE PLAN

PROSPECTUS SUPPLEMENT  
TO PROSPECTUS DATED AUGUST 22, 1996

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On August 14, 1998, Donegal Group Inc. (the "Company") filed with the Securities and Exchange Commission a Form 10-Q Quarterly Report for the quarter ended June 30, 1998, a copy of which, without exhibits, is attached to this Prospectus Supplement.

This Prospectus Supplement should be read in conjunction with the Company's Prospectus dated August 22, 1996 and the Company's 1997 Annual Report to Stockholders.

The date of this Prospectus Supplement is September 9, 1998.

Securities and Exchange Commission  
Washington, D.C. 20549  
Form 10-Q

(Mark One)

Quarterly Report Pursuant to Section 13 of the Securities Exchange Act of 1934

For the Quarterly Period Ended June 30, 1998

Transition Report Pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934

For the transition period from \_\_\_\_\_ to \_\_\_\_\_.

Commission File No. 0-15341

Donegal Group Inc.

-----  
(Exact name of registrant as specified in its charter)

Delaware

-----  
(State or other jurisdiction of incorporation or organization)

23-2424711

-----  
(I.R.S. Employer Identification No.)

1195 River Road, P.O. Box 302, Marietta, PA 17547-0302

-----  
(Address of principal executive offices, including zip code)

(717) 426-1931

-----  
(Registrant's telephone number, including area code)

-----  
(Former name, former address and former fiscal year, if changed since last report)

Indicate by check mark whether registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes x . No .  
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Applicable Only to Issuers Involved in Bankruptcy Proceedings During the Preceding Five Years:

Indicate by check mark whether the registrant has filed all documents and reports required by Sections 12, 13, or 15(d) of the Securities Exchange Act of 1934 subsequent to the distribution of securities under a plan confirmed by a court. Yes . No .  
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Applicable Only to Corporate Issuers:

Indicate the number of shares outstanding of each of the issuer's classes of common stock, as of the latest practicable date: 8,132,759 shares of Common Stock, \$1.00 par value, outstanding on July 31, 1998.

Part I. Financial Information

Item 1. Financial Statements.

Donegal Group Inc. And Subsidiaries  
Consolidated Balance Sheet

Assets	June 30, 1998	December 31, 1997
	-----	-----
Investments	(Unaudited)	
Fixed maturities		
Held to maturity, at amortized cost	\$113,012,794	\$117,246,205
Available for sale, at market value	63,681,171	57,731,251
Equity securities, available for sale at market	13,696,428	7,274,562
Short-term investments, at cost, which approximates market	13,663,713	22,712,787
Other investments, at cost, which approximates market	1,000,000	--
Total Investments	----- 205,054,106	----- 204,964,805
Cash	1,826,116	3,413,315
Accrued investment income	2,837,984	2,741,207
Premiums receivable	12,952,084	11,244,628
Reinsurance receivable	43,428,769	40,953,032
Deferred policy acquisition costs	9,109,754	8,448,060
Federal income tax receivable	459,059	56,454
Deferred federal income taxes	3,090,040	3,302,043
Prepaid reinsurance premiums	23,410,314	22,882,283
Property and equipment, net	5,058,747	4,938,524
Accounts receivable - securities	---	456,493
Due from affiliate	471,627	141,313
Other	1,270,007	562,348
Total Assets	----- \$308,968,607 =====	----- \$304,104,505 =====
Liabilities and Stockholders' Equity		
Liabilities		
Losses and loss expenses	\$122,566,123	\$118,112,390
Unearned premiums	74,728,962	71,367,691
Accrued expenses	2,310,911	3,214,767
Reinsurance balances payable	664,316	735,009
Cash dividend declared to stockholders	--	604,054
Line of credit	5,000,000	10,500,000
Accounts payable - securities	--	2,499,059
Other	611,826	283,098
Due to affiliate - Pioneer acquisition	5,191,774	5,191,774
Total Liabilities	----- 211,073,912	----- 212,507,842
Stockholders' Equity		
Preferred stock, \$1.00 par value, authorized 1,000,000 shares; none issued		
Common stock, \$1.00 par value, authorized 15,000,000 shares, issued 8,245,868 and 6,122,431 shares and outstanding 8,123,580 and 6,030,715 shares	8,245,868	6,122,431
Additional paid-in capital	40,187,679	38,932,117
Accumulated other comprehensive income	1,455,560	1,011,417
Retained earnings	48,897,344	46,422,454
Treasury stock	(891,756)	(891,756)
Total Stockholders' Equity	----- 97,894,695	----- 91,596,663
Total Liabilities and Stockholders' Equity	----- \$308,968,607 =====	----- \$304,104,505 =====

See accompanying notes to consolidated financial statements.

Donegal Group Inc. and Subsidiaries  
Consolidated Statement of Income  
(Unaudited)

For the three months ended June 30, 1998 and 1997

	Three Months Ended June 30, 1998	1997
	-----	-----
<b>Revenues:</b>		
Premiums earned	\$41,260,309	\$39,721,921
Premiums ceded	13,682,052	12,898,416
	-----	-----
Net premiums earned	27,578,257	26,823,505
Investment income, net of investment expenses	2,768,139	2,881,771
Realized gain	35,442	35,527
Lease income	188,120	154,396
Service charge income	453,068	358,661
	-----	-----
<b>Total Revenues</b>	<b>31,023,026</b>	<b>30,253,860</b>
	-----	-----
<b>Expenses:</b>		
Losses and loss expenses	28,433,598	25,799,082
Reinsurance recoveries	9,208,460	8,469,679
	-----	-----
Net losses and loss expenses	19,225,138	17,329,403
Amortization of deferred policy acquisition costs	5,025,000	4,251,000
Other underwriting expenses	3,450,366	4,605,054
Policy dividends	342,266	308,070
Interest	200,556	277,938
Other expenses	401,243	376,348
	-----	-----
<b>Total Expenses</b>	<b>28,644,569</b>	<b>27,147,813</b>
	-----	-----
Income before income taxes	2,378,457	3,106,047
Income taxes	485,025	705,450
	-----	-----
<b>Net income</b>	<b>\$ 1,893,432</b>	<b>\$ 2,400,597</b>
	=====	=====
<b>Earnings per common share</b>		
Basic	\$ .22	\$ .30*
	===	===
Diluted	\$ .22	\$ .30*
	===	===

Statement of Comprehensive Income  
(Unaudited)

	Three Months Ended June 30, 1998	1997
	-----	-----
Net Income	\$ 1,893,432	\$ 2,400,597
	-----	-----
Other comprehensive income, net of tax		
Unrealized gains on securities:		
Unrealized holding gain arising during the period	142,285	641,902
Less: Reclassification adjustment for losses included in Net income	(308)	(4,307)
	-----	-----
Other comprehensive income	141,977	637,595
	-----	-----
Comprehensive income	\$ 2,035,409	\$ 3,038,192
	=====	=====

\* Restated

See accompanying notes to consolidated financial statements.

Donegal Group Inc. and Subsidiaries  
Consolidated Statement of Income  
(Unaudited)

For the six months ended June 30, 1998 and 1997

	Six Months Ended June 30, 1998	1997
	-----	-----
Revenues:		
Premiums earned	\$81,739,088	\$78,763,105
Premiums ceded	26,956,287	25,535,267
	-----	-----
Net premiums earned	54,782,801	53,227,838
Investment income, net of investment expenses	5,613,406	5,726,754
Realized gain	347,235	73,354
Lease income	371,184	296,848
Service charge income	804,544	752,437
	-----	-----
Total Revenues	61,919,170	60,077,231
	-----	-----
Expenses:		
Losses and loss expenses	53,360,594	49,706,729
Reinsurance recoveries	18,333,551	15,464,783
	-----	-----
Net losses and loss expenses	35,027,043	34,241,946
Amortization of deferred policy acquisition costs	9,725,000	8,730,000
Other underwriting expenses	8,147,317	8,717,870
Policy dividends	820,124	741,769
Interest	383,615	442,925
Other expenses	823,052	773,813
	-----	-----
Total Expenses	54,926,151	53,648,323
	-----	-----
Income before income taxes	6,993,019	6,428,908
Income taxes	1,782,934	1,465,878
	-----	-----
Net income	\$5,210,085	\$ 4,963,030
	=====	=====
Earnings per common share		
Basic	\$ .63	\$ .62*
	===	===
Diluted	\$ .62	\$ .62*
	===	===

Statement of Comprehensive Income  
(Unaudited)

	Six Months Ended June 30, 1998	1997
	-----	-----
Net Income	\$ 5,210,085	\$ 4,963,030
	-----	-----
Other comprehensive income, net of tax		
Unrealized gains (losses) on securities:		
Unrealized holding gain arising during the period	486,787	128
Less: Reclassification adjustment for losses included in Net income	(41,644)	(717)
	-----	-----
Other comprehensive income (loss)	444,143	(589)
	-----	-----
Comprehensive income	\$ 5,654,228	\$ 4,962,441
	=====	=====

\* Restated

See accompanying notes to consolidated financial statements.

DONEGAL GROUP INC. AND SUBSIDIARIES  
CONSOLIDATED STATEMENT OF STOCKHOLDERS' EQUITY  
(Unaudited)  
FOR THE SIX MONTHS ENDED JUNE 30, 1998

	Common Stock		Additional Paid-In Capital	Accumulated Other Com- prehensive Income	Retained Earnings	Treasury Stock	Total Stock- holders' Equity
	Shares	Amount					
Balance, December 31, 1997	6,122,431	\$6,122,431	\$38,932,117	\$1,011,417	\$46,422,454	\$(891,756)	\$91,596,663
Issuance of Common Stock	61,970	61,970	1,255,562				1,317,532
Net Income					5,210,085		5,210,085
Other Comprehensive Income				444,143			444,143
Stock Dividend	2,061,467	2,061,467			(2,061,467)		--
Cash Dividend					(673,728)		(673,728)
Balance, June 30, 1998	<u>8,245,868</u>	<u>\$8,245,868</u>	<u>\$40,187,679</u>	<u>\$1,455,560</u>	<u>\$48,897,344</u>	<u>\$(891,756)</u>	<u>\$97,894,695</u>

See accompanying notes to consolidated financial statements.

DONEGAL GROUP INC. AND SUBSIDIARIES  
CONSOLIDATED STATEMENT OF CASH FLOWS  
(Unaudited)  
For the six months ended June 30, 1998 and 1997

	Six months ended 1998	June 30, 1997
	-----	-----
Cash Flows from Operating Activities:		
Net income	\$ 5,210,085	\$ 4,963,030
	-----	-----
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization	217,046	178,538
Realized investment gain	(347,235)	(73,354)
Changes in Assets and Liabilities:		
Losses and loss expenses	4,453,733	267,228
Unearned premiums	3,361,271	563,176
Premiums receivable	(1,707,456)	(15,611)
Deferred policy acquisition costs	(661,694)	(72,796)
Deferred federal income taxes	(16,798)	(110,876)
Reinsurance receivable	(2,475,737)	2,467,980
Prepaid reinsurance premiums	(528,031)	(515,112)
Accrued investment income	(96,777)	(151,078)
Due from affiliate	(330,314)	967,333
Reinsurance balances payable	(70,693)	(50,622)
Federal income taxes receivable	(402,605)	(795,418)
Other, net	(1,282,787)	(1,697,586)
	-----	-----
Net adjustments	111,923	961,802
	-----	-----
Net cash provided by operating activities	5,322,008	5,924,832
	-----	-----
Cash flows from investing activities:		
Purchase of fixed maturities		
Held to maturity	(9,004,828)	(13,087,963)
Available for sale	(14,234,581)	(10,183,672)
Purchase of equity securities, available for sale	(10,878,128)	(3,015,732)
Maturity of fixed maturities		
Held to maturity	13,307,736	4,484,420
Available for sale	5,248,065	3,594,999
Sale of fixed maturities - available for sale	535,765	4,010,313
Sale of equity securities, available for sale	5,893,013	1,538,232
Purchase of other investments	(1,000,000)	--
Purchase of property and equipment	(365,073)	(988,680)
Net sales of short-term investments	9,049,074	6,507,482
	-----	-----
Net cash used in investing activities	(1,448,957)	(7,140,601)
	-----	-----
Cash flows from financing activities:		
Cash dividends paid	(1,277,782)	(1,047,079)
Issuance of common stock	1,317,532	398,077
Line of credit, net	(5,500,000)	--
	-----	-----
Net cash provided by (used in) financing activities	(5,460,250)	(649,002)
	-----	-----
Net decrease in cash	(1,587,199)	(1,864,771)
Cash at beginning of year	3,413,315	3,700,163
	-----	-----
Cash at end of quarter	\$ 1,826,116	\$ 1,835,392
	=====	=====
Cash paid during period		
- Interest	\$ 58,143	\$ 334,014
- Income taxes	\$ 2,202,337	\$ 559,584

See accompanying notes to consolidated financial statements.

DONEGAL GROUP INC. AND SUBSIDIARIES  
(Unaudited)  
Summary Notes to Consolidated Financial Statements

1 - Organization

The Company was organized as a regional insurance holding company by Donegal Mutual Insurance Company (the "Mutual Company") on August 26, 1986 and operates in Pennsylvania, Maryland, Delaware, Virginia and Ohio through its wholly owned stock insurance companies, Atlantic States Insurance Company ("Atlantic States"), Southern Insurance Company of Virginia ("Southern"), Delaware Atlantic Insurance Company ("Delaware"), Pioneer Insurance Company ("Pioneer") and Atlantic Insurance Services, Inc. ("AIS"). The Company's major lines of business are Automobile Liability, Automobile Physical Damage, Homeowners, Commercial Multiple Peril and Workers' Compensation. Atlantic, Southern, Delaware and Pioneer are subject to regulation by Insurance Departments in those states in which they operate and undergo periodic examination by those departments. They are also subject to competition from other insurance carriers in their operating areas. Atlantic States engages in the insurance business primarily through an intercompany pooling arrangement with the Mutual Company. Southern was acquired by the Company on December 31, 1988 pursuant to a plan of conversion from a mutual to a stock company and cedes 50% of its business to the Mutual Company, 80% prior to 1991. On December 29, 1995, the Company acquired all of the outstanding stock of Delaware. This transaction was accounted for as if it were a "Pooling of Interest," and as such, the Company's financial statements have been restated to include Delaware as a consolidated subsidiary from January 1, 1994 to the present. On March 31, 1997, the Company acquired all of the outstanding stock of Pioneer. This transaction was accounted for as if it were a "Pooling of Interest", and as such the Company's financial statements have been restated to include Pioneer as a consolidated subsidiary from January 1, 1994 to the present. At June 30, 1998, the Mutual Company held 58% of the outstanding common stock of the Company.

2 - Basis of Presentation

The financial information for the interim period included herein is unaudited; however, such information reflects all adjustments, consisting only of normal recurring adjustments, which, in the opinion of management are necessary to a fair presentation of the financial position, results of operations and cash flow for the interim period included herein. The results of operations for the three months ended and for the six months ended June 30, 1998, are not necessarily indicative of results of operations to be expected for the twelve months ended December 31, 1998.

On June 25, 1998, the Company issued a 4 for 3 stock split in the form of a 33-1/3% stock dividend to stockholders of record as of June 10, 1998. Per share information prior to June 25, 1998, has been restated for this change.

These financial statements should be read in conjunction with the financial statements and notes thereto contained in the Registrant's Annual Report on Form 10-K for the year ended December 31, 1997.

Management's Discussion and Analysis of  
Financial Condition and Results of Operations

Overview

Donegal Group Inc. ("DGI" or the "Company") is a regional insurance holding company doing business in Pennsylvania, Maryland, Delaware, Virginia and Ohio through its four wholly owned property-casualty insurance subsidiaries, Atlantic States Insurance Company ("Atlantic"), Southern Insurance Company of Virginia ("Southern"), Pioneer Insurance Company ("Pioneer") and Delaware Atlantic Insurance Company ("Delaware"). The Company's major lines of business in 1997 and their percentage of total net earned premiums were Automobile Liability (27.8%), Workers' Compensation (15.9%), Automobile Physical Damage (17.1%), Homeowners (17.6%), and Commercial Multiple Peril (15.6%). The subsidiaries are subject to regulation by Insurance Departments in those states in which they operate and undergo periodic examination by those departments. The subsidiaries are also subject to competition from other insurance carriers in their operating areas. DGI was formed in September 1986 by Donegal Mutual Insurance Company (the "Mutual Company"), which owns 58% of the outstanding common shares of the Company as of June 30, 1998.

Atlantic States participates in an intercompany pooling arrangement with the Mutual Company and assumes 65% of the pooled business, 60% prior to January 1, 1996. Southern cedes 50% of its business to the Mutual Company and Delaware cedes 70% of its Workers' Compensation business to the Mutual Company. Because the Mutual Company places substantially all of the business assumed from Southern and Delaware into the pool, from which the Company has a 65% allocation, the Company's results of operations include approximately 80% of the business written by Southern and approximately 75% of the Workers' Compensation business written by Delaware.

In addition to the Company's insurance subsidiaries, it also owns all of the outstanding stock of Atlantic Insurance Services, Inc. ("AIS"), an insurance services organization currently providing inspection and policy auditing information on a fee for service basis to its affiliates and the insurance industry.

Results of Operations - Three Months Ended June 30, 1998 to Three Months Ended June 30, 1997

Revenues for the three months ended June 30, 1998 were \$31,023,026 an increase of \$769,166 or 2.5%, over the same period of 1997. An increase in net premiums earned of \$754,752 or 2.8%, represented most of this change. Investment income for the second quarter fell \$113,632 or 3.9% due to a decrease in the annualized average return on investments from 5.8% in the second quarter 1997 to 5.4% in the second quarter 1998, offset by an increase in average invested assets from \$197.2 million in the second quarter 1997 to \$205.0 million in the second quarter 1998. Realized investment gains, which resulted from normal turnover of the Company's investment portfolio, were \$35,442 in the second quarter 1998 compared to \$35,527 for the same period of 1997.

The GAAP combined ratio of insurance operations in the second quarter of 1998 was 101.7% compared to 98.8% for the same period in 1997. The GAAP combined ratio is the sum of the ratios of incurred losses and loss adjusting expenses to premiums earned (loss ratio), policyholders dividends to premiums earned (dividend ratio), and underwriting expenses to premiums earned (expense ratio). The Company's loss ratio was impacted by an unusual series of thunderstorms and tornadoes that hit the northeast part of the United States throughout the month of June, 1998. As a result of claims from these storms, the Company's loss ratio in the second quarter of 1998 was 69.7% compared to 64.6% in the second quarter of 1997. The increase in the loss ratio was somewhat offset by a decrease in the expense ratio to 30.7% in the second quarter of 1998 compared to 33.0% in the second quarter of 1997. This improvement was primarily due to decreases in incentive plans for employees and contingent commissions for agents due to the higher loss ratios. The dividend ratio changed little ending up at 1.3% for the second quarter of 1998 compared to 1.2% for the same period of 1997.

Federal income taxes for the second quarter represented 20.4% of income before income taxes compared to 22.7% for the same period of 1997. Decreased underwriting profits, due to the storm activity, resulted in tax free investment income representing a larger portion of income than in 1997 decreasing the effective tax rate.

Results of Operations - Six Months Ended June 30, 1998 to Six Months Ended June 30, 1997

Revenues for the six months ended June 30, 1998 were \$61,919,170 an increase of \$1,841,939 or 3.1%, over the same period of 1997. An increase in net premiums earned of \$1,554,963 represented most of this change. Investment income for the first six months fell \$113,348 or 2.0% due to a decrease in the annualized average return on investments from 5.8% for the first six months of 1997 to 5.4% for the first six months of 1998, offset by an increase in average invested assets from \$197.1 million in 1997 to \$207.6 million in the first six months of 1998. Realized investment gains, which resulted from normal turnover of the Company's investment portfolio, were \$347,235 in the six months ended June 30, 1998 compared to \$73,354 for the same period of 1997.

The GAAP combined ratio of insurance operations for the six months ended June 30, 1998 was 98.1 % compared to 98.5% for the same period in 1997. The GAAP combined ratio is the sum of the ratios of incurred losses and loss adjusting expenses to premiums earned (loss ratio), policyholders dividends to premiums earned (dividend ratio), and underwriting expenses to premiums earned (expense ratio). The Company's loss ratio was impacted by an unusual series of thunderstorms and tornadoes that hit the northeast part of the United States throughout the month of June, 1998 but had been favorably effected by the mild winter weather in the same part of the country in the first quarter. As a result, the Company's loss ratio for the first six months of 1998 was 63.9% compared to 64.3% for the first six months of 1997. The expense ratio for the six months ended June 30, 1998 was 32.6%, almost identical to the 32.8% expense ratio for the same period of 1997. The dividend ratio changed little ending up at 1.5% for the period compared to 1.4% for the first six months of 1997.

Federal income taxes for the first six months of 1998 represented 25.5% of income before income taxes compared to 22.8% for the same period of 1997. Tax savings from the acquisition of Pioneer last year accounted for the difference.

## Liquidity and Capital Resources

The Company generates sufficient funds from its operations and maintains a high degree of liquidity in its investment portfolio. The primary source of funds to meet the demands of claim settlements and operating expenses are premium collections, investment earnings and maturing investments. As of June 30, 1998, the Company had announced it has entered into an agreement to purchase all of the outstanding shares of Southern Heritage Insurance Company, Tucker, Georgia, for \$21 million in cash. The acquisition is pending regulatory approval. The Company has requested an amendment to its credit agreement with Fleet Bank to expand the credit available under that agreement from \$20 million to \$40 million to fund the acquisition.

In investing funds made available from operations, the Company maintains securities maturities consistent with its projected cash needs for the payment of claims and expenses. The Company maintains a portion of its investment portfolio in relatively short-term and highly liquid assets to ensure the availability of funds.

As of June 30, 1998, pursuant to a credit agreement dated December 29, 1995, with Fleet National Bank of Connecticut, the Company had unsecured borrowings of \$5.0 million. Per the terms of the credit agreement, the Company may borrow up to \$20 million at interest rates equal to the bank's then current prime rate or the then current London interbank Eurodollar bank rate plus 1.70%. At June 30, 1998, the interest rate on the outstanding balance was 7.60625%. In addition, the Company will pay a non-use fee at a rate of 3/10 of 1% per annum on the average daily unused portion of the Bank's commitment. On each December 29, commencing December 29, 1999, the credit line will be reduced by \$4 million. Any outstanding loan in excess of the remaining credit line, after such reduction, will then be payable.

The Company's principal source of cash with which to pay stockholder dividends is dividends from Atlantic States, Southern, Pioneer and Delaware, which are required by law to maintain certain minimum surplus on a statutory basis and are subject to regulations under which payment of dividends from statutory surplus is restricted and may require prior approval of their domiciliary insurance regulatory authorities. Atlantic States, Southern, Pioneer and Delaware are subject to Risk Based Capital (RBC) requirements effective for 1994. At December 31, 1997, all four Companies' capital was substantially above the RBC requirements. At December 31, 1997, amounts available for distribution as dividends to Donegal Group without prior approval of the insurance regulatory authorities are \$7,349,284 from Atlantic States, \$703,688 from Southern, \$542,799 from Pioneer and \$1,070,463 from Delaware.

## Credit Risk

The company provides property and liability coverages through its subsidiaries' independent agency systems located throughout its operating area. The majority of this business is billed directly to the insured although a portion of Donegal Group's commercial business is billed through its agents who are extended credit in the normal course of business.

The Company's subsidiaries have reinsurance agreements in place with the Mutual Company and with a number of other major authorized reinsurers.

## Impact of Inflation

Property and casualty insurance premiums are established before the amount of losses and loss settlement expenses, or the extent to which inflation may impact such expenses, are known. Consequently, the Company attempts, in establishing rates, to anticipate the potential impact of inflation.

## Year 2000 Issues

The year 2000 issue (i.e. the ability of computer systems to properly process information which contains dates beginning with January 1, 2000 and thereafter) affects virtually all companies. All computer systems used for processing of business for the Company are owned and operated by the Mutual Company. Certain of these computer systems utilized by the Mutual Company to process information use only two digits to identify a year. Because of this, the year 2000 would be represented in the system as "00" and would in most cases be interpreted by the computer as "1900" rather than "2000", resulting in processing errors.

The ability to process information in a timely and accurate manner is vital to the Company's property and casualty insurance business. The Company recognizes that the systems used to process its business must be able to accurately identify and process information containing year 2000 dates by the end of 1998. The Mutual Company has a vigorous and comprehensive project underway to ensure compliance in time to meet this deadline. This project was initiated as part of a review of the main application systems in 1995. The Mutual Company is taking the steps it deems appropriate to meet this challenge, including migrating to the most current version of vendors' software, which improves functionality in addition to being year 2000 compliant, replacing existing software with new software systems and rewriting existing computer programs. The goal of this project is to be substantially year 2000 compliant by the end of 1998.

## Impact of New Accounting Standards

### Accounting for Derivative Instruments and Hedging Activities

In June, 1998, the Financial Accounting Standards Board issued SFAS No. 133, "Accounting for Derivative Instruments and Hedging Activities". SFAS No. 133 establishes accounting and reporting standards for derivative instruments and for hedging activities. SFAS No. 133 is effective for fiscal years beginning after June 15, 1999, with earlier adoption permitted.

## Insurance Related Assessments

In December 1997, the AICPA Accounting Standards Executive Committee issued Statement of Position (SOP) 97-3, Accounting by Insurance and Other Enterprises for Insurance-Related Assessments. The accounting guidance of this SOP focuses on the timing of recognition and measurement of liabilities for insurance-related assessments. The SOP is effective for fiscal years beginning after December 15, 1998. The Company believes that they are in compliance with the provisions of this SOP and no impact on the Company's financial reporting is expected.

#### Computer Software Development Costs

On March 4, 1998, the AICPA Accounting Standards Executive Committee issued Statement of Position (SOP) 98-1, Accounting for the Costs of Computer Software Developed or Obtained for Internal Use. This SOP requires that certain costs related to the development or purchase of internal-use software be capitalized and amortized over the estimated useful life of the software. This SOP also requires that costs related to the preliminary project stage and the post-implementation/operations stage in an internal-use computer software development project be expensed as incurred. SOP 98-1 is effective for financial statements issued for fiscal years beginning after December 15, 1998. The Company believes that they are in compliance with the provisions of this SOP and no material impact of the Company's financial reporting is expected.

Part II. Other Information

Item 1. Legal Proceedings

None.

Item 2. Changes in Securities

Amendment of Certificate of Incorporation  
Exhibit 3(i)

Item 3. Defaults upon Senior Securities

None.

Item 4. Submission of Matters to a Vote of Security Holders

None.

Item 5. Other Information

Any stockholder who, in accordance with and subject to the provisions of the proxy rules of the Securities and Exchange Commission, wishes to submit a proposal for inclusion in the Company's proxy statement for its 1999 Annual Meeting of Stockholders must deliver such proposal in writing to the Company's Secretary at the Company's principal executive offices at 1195 River Road, Marietta, Pennsylvania 17547, not later than November 23, 1998.

Pursuant to new amendments to Rule 14a-4(c) of the Securities Exchange Act of 1934, if a stockholder who intends to present a proposal at the 1999 Annual Meeting of Stockholders does not notify the Company of such proposal on or before February 7, 1999, then management proxies will be allowed to use their discretionary voting authority to vote on the proposal when the proposal is raised at the Annual Meeting, even though there is no discussion of the proposal in the 1999 proxy statement.

Item 6. Exhibits and Reports on Form 8-K

- (a) EX-27 Financial Data Schedule
- (b) Reports on Form 8-K  
During the quarter ended June 30, 1998 - None

Signatures

Pursuant to the requirements of the Securities Exchange Act of 1934, the Registrant has duly caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

Donegal Group Inc.

Date: August 14, 1998

By: -----  
Donald H. Nikolaus,  
President and Chief Executive Officer

Date: August 14, 1998

By: -----  
Ralph G. Spontak,  
Corporate Secretary,  
Senior Vice President and  
Chief Financial Officer

3-MOS

DEC-31-1998  
JUN-30-1998  
63,681,171  
113,012,794  
116,588,112  
13,663,713  
0  
2,496,510  
205,054,106  
1,826,116  
0  
9,109,754  
308,968,607  
122,566,123  
74,728,962  
0  
0  
5,000,000  
0  
0  
8,245,868  
97,894,695  
308,968,607  
54,782,801  
5,613,406  
347,235  
1,175,728  
35,027,043  
9,725,000  
8,147,317  
6,993,019  
1,782,934  
5,210,085  
0  
0  
0  
5,210,085  
.63  
.62  
77,474  
36,830  
(1,803)  
22,014  
11,350  
79,137  
(1,803)