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

(Mark One)

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

For the Quarterly Period Ended June 30, 2000

or

[ ] 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 | 23-2424711 |
| (State or other jurisdiction of incorporation or organization) | (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 .

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 .

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: 8,732,837 shares of Common Stock, $1.00 par value, outstanding on July 31, 2000.

# Part I. Financial Information

## Item 1. Financial Statements.

Donegal Group Inc. And Subsidiaries
Consolidated Balance Sheet

| Assets | June 30, 2000 | December 31, 1999 |
|---|---|---|
| Investments | (Unaudited) | |
| Fixed maturities | | |
| Held to maturity, at amortized cost | $136,587,402 | $136,173,547 |
| Available for sale, at fair value | 105,264,515 | 100,043,548 |
| Equity securities, available for sale at fair value | 13,377,106 | 9,229,498 |
| Short-term investments, at cost, which approximates fair value | 11,891,757 | 15,995,257 |
| Total Investments | 267,120.780 | 261,441,850 |
| Cash | 1,661,701 | 3,922,403 |
| Accrued investment income | 3,638,159 | 3,474,430 |
| Premiums receivable | 21,716,434 | 18,218,525 |
| Reinsurance receivable | 53,777,534 | 53,070,283 |
| Deferred policy acquisition costs | 11,771,006 | 11,203,302 |
| Federal income tax receivable | 619,028 | 698,969 |
| Deferred federal income taxes | 8,775,722 | 9,121,232 |

| | | |
|---|---|---|
| Prepaid reinsurance premiums | 36,850,275 | 32,154,837 |
| Property and equipment, net | 5,226,538 | 5,516,688 |
| Due from affiliate | 364,796 | 262,954 |
| Other | 691,369 | 647,184 |
| Total Assets | $412,253,342 | $399,732,657 |
| Liabilities and Stockholders' Equity | | |
| Liabilities | | |
| Losses and loss expenses | $152,538,908 | $149,979,141 |
| Unearned premiums | 106,298,817 | 97,657,020 |
| Accrued expenses | 4,906,800 | 5,888,392 |
| Drafts payable | 108,628 | 597,775 |
| Reinsurance balances payable | 947,842 | 1,216,034 |
| Cash dividend declared to stockholders | -- | 760,673 |
| Line of credit | 37,000,000 | 37,000,000 |
| Accounts payable - securities | 1,100,000 | 2,500,000 |
| Other | 1,352,672 | 719,010 |
| Total Liabilities | 304,253,667 | 296,318,045 |
| Stockholders' Equity | | |
| Preferred stock, $1.00 par value, authorized 1,000,000 shares; none issued | | |
| Common stock, $1.00 par value, authorized 10,000,000 shares, issued 8,833,411 and 8,574,210 shares and outstanding 8,711,123 and 8,451,922 shares | 8,833,411 | 8,574,210 |
| Additional paid-in capital | 44,993,241 | 43,536,748 |
| Accumulated other comprehensive loss | (2,138,806) | (2,073,989) |
| Retained earnings | 57,203,585 | 54,269,399 |
| Treasury stock | (891,756) | (891,756) |
| Total Stockholders' Equity | 107,999,675 | 103,414,612 |
| Total Liabilities and Stockholders' Equity | $412,253,342 | $399,732,657 |

See accompanying notes to consolidated financial statements.

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

| | Three Months Ended June 30, 2000 | 1999 |
|---|---|---|
| Revenues: | | |
| Premiums earned | $ 54,582,537 | $ 52,653,705 |
| Premiums ceded | 18,559,888 | 16,823,890 |
| Net premiums earned | 36,022,649 | 35,829,815 |
| Investment income, net of investment expenses | 3,798,470 | 3,155,817 |
| Realized gains | 391,117 | 32,345 |
| Lease income | 208,222 | 205,224 |
| Service charge income | 381,142 | 564,786 |
| Total Revenues | 40,801,600 | 39,787,987 |
| Expenses: | | |
| Losses and loss expenses | 36,790,924 | 36,505,254 |
| Reinsurance recoveries | 12,185,174 | 12,342,954 |
| | 24,605,750 | 24,162,300 |
| Amortization of deferred policy acquisition costs | 6,117,000 | 7,325,000 |
| Other underwriting expenses | 5,519,476 | 5,763,127 |
| Policy dividends | 234,273 | 298,636 |
| Interest | 757,778 | 263,487 |
| Other expenses | 294,120 | 478,571 |
| Total Expenses | 37,528,397 | 38,291,121 |
| Income before income taxes | 3,273,203 | 1,496,866 |
| Income tax | 802,803 | 196,130 |
| Net income | $ 2,470,400 | $ 1,300,736 |
| Earnings per common share | | |
| Basic | $ 0.28 | $ 0.16 |
| Diluted | $ 0.28 | $ 0.16 |

Statement of Comprehensive Income
(Unaudited)

Three Months Ended June 30,

| | 2000 | 1999 |
|---|---|---|
| Net Income | $ 2,470,400 | $ 1,300,736 |
| Other comprehensive loss, net of tax | | |
| Unrealized gains on securities: | | |
| Unrealized holding gain (loss) during the period | 492,943 | (1,419,048) |
| Less: Reclassification adjustment for gains included in net income, net of income tax | (258,138) | (21,348) |
| Other comprehensive income (loss) | 234,805 | (1,440,396) |
| Comprehensive income (loss) | $ 2,705,205 | $ (139,660) |

See accompanying notes to consolidated financial statements.

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

| | Six Months Ended June 30, 2000 | Six Months Ended June 30, 1999 |
|---|---|---|
| Revenues: | | |
| Premiums earned | $107,876,185 | $104,489,888 |
| Premiums ceded | 36,268,443 | 32,566,102 |
| Net premiums earned | 71,607,742 | 71,923,786 |
| Investment income, net of investment expenses | 7,675,839 | 6,525,078 |
| Realized gain | 109,207 | 15,415 |
| Lease income | 414,994 | 404,361 |
| Service charge income | 739,352 | 1,031,337 |
| Total Revenues | 80,547,134 | 79,897,977 |
| Expenses: | | |
| Losses and loss expenses | 74,718,250 | 73,106,709 |
| Reinsurance recoveries | 24,574,508 | 24,492,758 |
| | 50,143,742 | 48,613,951 |
| Amortization of deferred policy acquisition costs | 12,188,000 | 13,356,000 |
| Other underwriting expenses | 10,540,088 | 11,520,884 |
| Policy dividends | 587,235 | 630,012 |
| Interest | 1,580,988 | 694,431 |
| Other expenses | 568,007 | 860,958 |
| Total Expenses | 75,608,060 | 75,676,236 |
| Income before income taxes | 4,939,074 | 4,221,741 |
| Income taxes | 1,218,440 | 769,638 |
| Net income | $ 3,720,634 | $ 3,452,103 |
| Earnings per common share | | |
| Basic | $ 0.43 | $ 0.42 |
| Diluted | $ 0.43 | $ 0.42 |

Consolidated Statement of Comprehensive Income
(Unaudited)

| | Six Months Ended June 30, 2000 | Six Months Ended June 30, 1999 |
|---|---|---|
| Net Income | $ 3,720,634 | $ 3,452,103 |
| Other comprehensive loss, net of tax | | |
| Unrealized gains on securities: | | |
| Unrealized holding gain (loss) during the period | 7,260 | (2,209,513) |
| Less: Reclassification adjustment for gains included in net income, net of income tax | (72,077) | (10,174) |
| Other comprehensive loss | (64,817) | (2,219,687) |
| Comprehensive income | $ 3,655,817 | $ 1,232,416 |

See accompanying notes to consolidated financial statements.

DONEGAL GROUP INC. AND SUBSIDIARIES
CONSOLIDATED STATEMENT OF STOCKHOLDERS' EQUITY
(Unaudited)
FOR THE THREE MONTHS ENDED JUNE 30, 2000

| | Common Stock | | | | | | |
|---|---|---|---|---|---|---|---|
| | Shares | Amount | Additional Paid-In Capital | Accumulated Other Comprehensive Loss | Retained Earnings | Treasury Stock | Total Stockholders' Equity |
| Balance, December 31, 1999 | 8,574,210 | $ 8,574,210 | $ 43,536,748 | $ (2,073,989) | $ 54,269,399 | $(891,756) | $ 103,414,612 |
| Issuance of Common Stock | 259,201 | 259,201 | 1,456,493 | | | | 1,715,694 |
| Net Income | | | | | 3,720,634 | | 3,720,634 |
| Cash Dividend | | | | | (786,448) | | (786,448) |
| Other Comprehensive Loss | | | | (64,817) | | | (64,817) |
| Balance, June 30, 2000 | 8,833,411 | $ 8,833,411 | $ 44,993,241 | $ (2,138,806) | $ 57,203,585 | $(891,756) | $ 107,999,675 |

See accompanying notes to consolidated financial statements.

DONEGAL GROUP INC. AND SUBSIDIARIES
CONSOLIDATED STATEMENT OF CASH FLOWS
(Unaudited)

| | Six Months Ended June 30, 2000 | 1999 |
|---|---|---|
| Cash flows from operating activities: | | |
| Net income | $ 3,720,634 | $ 3,452,103 |
| Adjustments to reconcile net income to net cash provided by operating activities: | | |
| Depreciation and amortization | 459,357 | 545,699 |
| Realized investment gain | (109,207) | (15,415) |
| Changes in assets and liabilities: | | |
| Losses and loss expenses | 2,559,767 | 2,326,730 |
| Unearned premiums | 8,641,797 | 7,430,128 |
| Premiums receivable | (3,497,909) | (3,146,764) |
| Deferred policy acquisition costs | (567,704) | (426,936) |
| Deferred income taxes | 323,613 | (171,058) |
| Reinsurance receivable | (707,251) | (1,975,318) |
| Prepaid reinsurance premiums | (4,695,438) | (4,548,994) |
| Accrued investment income | (163,729) | (400,732) |
| Due from affiliate | (101,842) | 1,182,782 |
| Reinsurance balances payable | (268,192) | (337,913) |
| Current income taxes | 79,941 | 3,200 |
| Other, net | (904,820) | (422,928) |
| Net adjustments | 1,048,383 | 42,481 |
| Net cash provided by operating activities | 4,769,017 | 3,494,584 |
| Cash flows from investing activities: | | |
| Purchase of fixed maturities | | |
| Held to maturity | (5,810,028) | (8,727,038) |
| Available for sale | (12,694,530) | (13,639,230) |
| Purchase of equity securities, available for sale | (13,470,191) | (7,162,651) |
| Maturity of fixed maturities | | |
| Held to maturity | 6,175,468 | 10,150,310 |
| Available for sale | 4,700,000 | 10,154,868 |
| Sale of fixed maturities, available for sale | 496,250 | -- |
| Sale of equity maturities, available for sale | 9,440,407 | 967,504 |
| Purchase of property and equipment | (139,168) | (789,563) |
| Net sales of short-term investments | 4,103,500 | 22,697,512 |
| Net cash provided by (used in) investing activities | (7,198,292) | 13,651,712 |
| Cash flows from financing activities: | | |
| Cash dividends paid | (1,547,121) | (1,442,326) |
| Issuance of common stock | 1,715,694 | 1,263,673 |
| Line of credit, net | -- | (22,500,000) |
| Net cash provided by (used in) financing activities | 168,573 | (22,678,653) |
| Net decrease in cash | (2,260,702) | (5,532,357) |
| Cash at beginning of period | 3,922,403 | 8,227,042 |
| Cash at end of period | $ 1,661,701 | $ 2,694,685 |
| Cash paid during period - Interest | $ 1,102,693 | $ 700,279 |
| Net cash received during period - Income taxes | $ 810,456 | $ 595,380 |

See accompanying notes to consolidated financial statements.

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

1 - Organization

Donegal Group Inc. (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 the Mid-Atlantic and Southern states through its wholly-owned stock insurance companies, Atlantic States Insurance Company ("Atlantic States"), Southern Heritage Insurance Company ("Southern Heritage"), Southern Insurance Company of Virginia ("Southern"), Delaware Atlantic Insurance Company ("Delaware") and Pioneer Insurance Company ("Pioneer") ( collectively "Insurance Subsidiaries"). The Company has three operating segments: the investment function, the personal lines of insurance and the commercial lines of insurance. Products offered in the personal lines of insurance consist primarily of homeowners and private passenger automobile policies. Products offered in the commercial lines of insurance consist primarily of commercial automobile, commercial multiple peril and workers' compensation policies. The Insurance Subsidiaries are subject to regulation by Insurance Departments in those states in which they operate and undergo periodic examinations by those departments. The Insurance Subsidiaries are also subject to competition from other insurance companies in their operating areas. Atlantic States participates in an inter-company pooling arrangement with the Mutual Company and assumed 65% of the pooled business. Effective July 1, 2000 the pooling arrangement was amended changing Atlantic States' portion of the pooled business to 70%. Southern cedes 50% of its business to the Mutual Company. At June 30, 2000, the Mutual Company held 62% of the outstanding common stock of the Company.

The Company and Donegal Mutual have been granted approval from the Federal Office of Thrift Supervision to form a savings bank. The bank will be 40% owned by the Company and 60% by Donegal Mutual and will require that the Company contribute approximately $2.8 million in start up capital. It is currently anticipated that the thrift will be formed in and open for business in the third quarter of this year.

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 and six months ended June 30, 2000, are not necessarily indicative of results of operations to be expected for the twelve months ended December 31, 2000.

As interim period financial statements, these financial statements do not include all of the information and footnotes required by generally accepted accounting principles for complete financial statements. As such, 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, 1999.

3 - Earnings Per Share

The computation of basic and diluted earnings per share is as follows:

| | Net Income | Weighted Average Shares Outstanding | Earnings Per Share |
|---|---|---|---|
| Three Months Ended June 30: | | | |
| 2000 | | | |
| Basic | $2,470,400 | 8,680,348 | $ .28 |
| Effect of stock options | -- | -- | -- |
| Diluted | $2,470,400 | 8,680,348 | $ .28 |
| 1999 | | | |
| Basic | $1,300,736 | 8,292,407 | $ .16 |
| Effect of stock options | -- | -- | -- |
| Diluted | $1,300,736 | 8,292,407 | $ .16 |
| Six Months Ended June 30: | | | |
| 2000 | | | |
| Basic | $3,720,634 | 8,626,365 | $ .43 |
| Effect of stock options | -- | -- | -- |
| Diluted | $3,720,634 | 8,626,365 | $ .43 |
| 1999 | | | |
| Basic | $3,452,103 | 8,264,995 | $ .42 |
| Effect of stock options | -- | -- | -- |
| Diluted | $3,452,103 | 8,264,995 | $ .42 |

The following options to purchase shares of common stock were not included in the computation of diluted earnings per share because the exercise price of the options was greater than the average market price:

| | For The Three Months Ended June 30, | | For The Six Months Ended June 30, | |
|---|---|---|---|---|
| | 2000 | 1999 | 2000 | 1999 |
| Number of Options | 1,425,281 | 1,011,116 | 1,425,281 | 1,011,116 |

4 - Segment Information

The Company evaluates the performance of the personal lines and commercial lines based upon underwriting results as determined under statutory accounting practices (SAP) which is used by management to measure performance for the total business of the Company.

Financial data by segment is as follows:

| | Three Months Ended June 30 2000 | 1999 |
|---|---|---|
| | ($ in thousands) | |
| Revenues: | | |
| Premiums earned: | | |
| Commercial lines | $12,903 | $11,797 |
| Personal lines | 23,120 | 24,033 |
| Total net premiums earned | 36,023 | 35,830 |
| Net investment income | 3,799 | 3,156 |
| Realized investment Gains | 391 | 32 |
| Other | 588 | 770 |
| Total revenues | $40,801 | $39,788 |
| Income before income taxes: | | |
| Underwriting income (loss) | | |
| Commercial lines | $ 995 | $ 416 |
| Personal lines | (2,158) | (2,791) |
| SAP underwriting loss | (1,163) | (2,375) |
| GAAP adjustments | 709 | 656 |
| GAAP underwriting loss | (454) | (1,719) |
| Net investment income | 3,799 | 3,156 |
| Realized investment losses | 391 | 32 |
| Other | (463) | 28 |
| Income before income taxes | $ 3,273 | $ 1,497 |

| | Six Months Ended June 30 2000 | 1999 |
|---|---|---|
| | ($ in thousands) | |
| Revenues: | | |
| Premiums earned: | | |
| Commercial lines | $25,302 | $23,182 |
| Personal lines | 46,306 | 48,742 |
| Total net premiums earned | 71,608 | 71,924 |
| Net investment income | 7,676 | 6,525 |
| Realized investment Gains | 109 | 15 |
| Other | 1,154 | 1,434 |
| Total revenues | $80,547 | $79,898 |
| Income before income taxes: | | |
| Underwriting income (loss) | | |
| Commercial lines | $ 100 | $ (205) |
| Personal lines | (2,628) | (2,169) |
| SAP underwriting loss | (2,528) | (2,374) |
| GAAP adjustments | 677 | 177 |
| GAAP underwriting loss | (1,851) | (2,197) |
| Net investment income | 7,676 | 6,525 |
| Realized investment losses | 109 | 15 |
| Other | (995) | (121) |
| Income before income taxes | $ 4,939 | $ 4,222 |

5 - Restructuring Charge

On September 29, 1999, the Company announced a plan to consolidate certain subsidiary support functions into its Marietta, Pennsylvania office. As a result of this consolidation, the Company recorded a restructuring charge in 1999 of $2,044,000 for employee termination benefits, occupancy charges, lease cancellation costs, and asset impairments. The charge was included in other underwriting expenses. The consolidation has been completed.

Employee termination benefits include severance payments, which were paid either in a lump sum or over a defined period, and related benefits for approximately 60 employees. Of the terminated employees, approximately 50% were from subsidiary support functions and approximately 50% were from the Marietta, Pennsylvania office. By December 31, 1999, all of the terminated employees had left the employment of the Company.

Included in occupancy charges are future lease obligations, less anticipated sublease benefits, for leased space which is no longer being used by the Delaware and Southern Heritage subsidiary support functions.

Also included in the restructuring charges were contract cancellation costs that represented the estimated cost to buy out of the remaining term on printer, copier, and computer processing contracts that provided no future benefits to the Company as a result of the restructuring. By December 31, 1999 all such assets had been taken out of service.

Asset impairments, which were a direct result of the consolidation of subsidiary functions, amounted to $407,000. They consisted of capitalized programming and data center costs, voice systems, and leasehold and office improvements. These assets were written-down to zero in 1999. By December 31, 1999 all such assets were taken out of service.

Activity in the restructuring accrual is as follows:

| | Employee Termination Benefits | Occupancy | Contract Cancellations | Totals |
|---|---|---|---|---|
| BALANCE AT 12/31/99 | $ 368,000 | $ 441,000 | $ 73,000 | $ 882,000 |
| CASH PAYMENTS | (317,000) | (88,000) | (73,000) | (478,000) |
| BALANCE AT 6/30/00 | $ 51,000 | $ 353,000 | $ -- | $ 404,000 |

Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations

Results of Operations -Three Months Ended June 30, 2000 to Three Months Ended June 30, 1999

Revenues for the three months ended June 30, 2000 were $40,801,600 an increase of $1,013,613 or 2.5%, over the same period of 1999. An increase in investment income of $642,653, or 20.4% coupled with an increase in realized gains of $358,772 represented most of this change. in investment income. An increase in the annualized average return on investments from 5.3% in the second quarter of 1999 to 5.8% in the second quarter of 2000 and an increase in average invested assets from $238.6 million in the second quarter of 1999 to $260.0 million in the second quarter of 2000, accounted for most of the change. Net premiums earned increased $192,834 or 0.5%. Premiums earned of Southern Heritage Insurance Company decreased $1.7 million as part of the reunderwriting of its book of business. This decrease was more than offset by an increase of $1.9 million, or 5.4% in the earned premiums of the Company's other subsidiaries. The realized losses in the second quarter of both 2000 and 1999 resulted from the normal turnover of the Company's investment portfolio.

The GAAP combined ratio of insurance operations in the second quarter of 2000 was 101.3% compared to 104.8% for the same period in 1999. 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 in the second quarter of 2000 was 68.3% compared to 67.4% for the same period of 1999. The loss ratio increase resulted primarily from an increase in frequency related to catastrophe type losses in the second quarter of 2000. The increase in the loss ratio was more than offset by an improvement in the expense ratio for the second quarter of 2000 to 32.3% compared to 36.5% for the second quarter of 1999. The improvement in the expense ratio resulted primarily from the Company's previously announced restructuring plan that was implemented at the end of the third quarter of 1999. The dividend ratio remained virtually unchanged at 0.7% for the second quarter of 2000 compared to 0.8% for the same period of 1999.

Federal income taxes for the three months ended June 30, 2000 represented 24.5% of the income before income taxes compared to 13.1% for the same period of 1999. These rates vary from the expected rate of 34% primarily due to the effect of tax exempt investment income which represented a higher percentage of net income in second quarter of 1999 compared to the second quarter of 2000.

Results of Operations - Six Months Ended June 30, 2000
to Six Months Ended June 30, 1999

Revenues for the six months ended June 30, 2000 were $80,547,134 an increase of $649,157 or 0.8%, over the same period of 1999. An increase in investment income of $1,150,761, or 17.6%, offset by a decrease in service charge income of $291,985 and a decrease in net premiums earned of $316,044, accounted for the change. An increase in the annualized average return on investments from 5.3% in the first six months of 1999 to 5.8% in the first six months of 2000 and an increase in average invested assets from $246.7 million in the first six months of 1999 to $264.3 million in the first six months of 2000, accounted for the change in investment income. Premiums earned of Southern Heritage Insurance Company decreased $4.1 million as part of the reunderwriting of its book of business. This decrease was mostly offset by an increase of $3.8 million, or 6.5% in the earned premiums of the Company's other subsidiaries.

The GAAP combined ratio of insurance operations in the first six of 2000 was 102.6% compared to 103.1% for the same period in 1999. 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 in the first six months of 2000 was 70.0% compared to 67.6% for the same period of 1999. The loss ratio increase resulted primarily from an increase in frequency related to catastrophe type losses in the second quarter of 2000 and from deterioration in results from private passenger automobile and workers' compensation lines of business during the first quarter of 2000. The increase in the loss ratio was more than offset by an improvement in the expense ratio for the first six months of 2000 to 31.7% compared to 34.6% for the same period of 1999. The improvement in the expense ratio resulted primarily from the Company's previously announced restructuring plan that was implemented at the end of the third quarter in 1999. The dividend ratio remained virtually unchanged at 0.8% for the first half of 2000 compared to 0.9% for the same period of 1999.

Federal income taxes for the six months ended June 30, 2000 represented 24.7% of the income before income taxes compared to 18.2% for the same period of 1999. These rates vary from the expected rate of 34% primarily due to the effect of tax exempt investment income which represented a higher percentage of net income in first half of 1999 compared to the first half of 2000.

## 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. The Company will be required to contribute $2.8 million in capital as part of the formation of a thrift for which it and Donegal Mutual have been granted approval from the Federal Office of Thrift Supervision. The capital contribution will take place in the third quarter of this year.

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, 2000, pursuant to a credit agreement dated December 29, 1995, with Fleet National Bank of Connecticut, (the " Bank") the Company had unsecured borrowings of $37.0 million. Per the terms of the credit agreement, the Company may borrow up to $40 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, 2000, the interest rates on the outstanding balances were 7.9% on an outstanding eurodollar balance of $22.0 million and 8.1% on an outstanding eurodollar rate balance of $15.0 million. 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 July 27, commencing July 27, 2001, the credit line will be reduced by $8 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, Southern Heritage 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, Southern Heritage and Delaware are subject to Risk Based Capital (RBC) requirements. At December 31, 1999, each of the five Companies' capital was substantially above the RBC requirements. At December 31, 1999, amounts available for distribution as dividends to Donegal Group without prior approval of the insurance regulatory authorities are $6,851,802 from Atlantic States, $184,285 from Southern, $567,793 from Pioneer, $956,381 from Delaware and $1,650,842 from Southern Heritage.

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.

## Part II. Other Information

Item 1. Legal Proceedings.

None.

Item 2. Changes in Securities.

None.

Item 3. Defaults upon Senior Securities.

Quantitative and Qualitative Disclosure About Market Risk

The Company's market risk generally represents the risk of gain or loss that may result from the potential change in the fair value of the Company's investment portfolio as a result of fluctuations in prices and interest rates and, to a lesser extent, its debt obligations. The Company attempts to manage its interest rate risk by maintaining an appropriate relationship between the average duration of the investment portfolio and the approximate duration of its liabilities, i.e., policy claims and debt obligations.

The Company has maintained approximately the same duration of its investment portfolio to its liabilities from December 31, 1999 to June 30, 2000. In addition, the Company has maintained approximately the investment mix during this period.

There have been no material changes to the Company's quantitative or qualitative market risk exposure from December 31, 1999 through June 30, 2000.

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

None.

Item 5. Other Information.

None.

Item 6. Exhibits and Reports on Form 8-K.

(a) EX -27 Financial Data Schedule
(b) Reports on 8-K:

A form 8-K was filed on June 19, 2000 reporting the changes in the pooling agreement between Atlantic States Insurance Company and Donegal Mutual Insurance Company.

## 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.

August 11, 2000

By:____________________________________

Donald H. Nikolaus, President
and Chief Executive Officer

August 11, 2000

By:___________________________________________

Ralph G. Spontak, Senior Vice President,
Chief Financial Officer and Secretary

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3-MOS
DEC-31-2000
JUN-30-2000
105,264,515
136,587,402
134,454,830
13,377,106
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2,432,053
267,120,780
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152,538,908
106,298,817
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0
37,000,000
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0
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412,253,342
71,607,742
7,675,839
109,207
1,154,346
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12,188,000
10,540,088
4,939,074
1,218,440
3,720,634
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0
3,720,634
.43
.43
97,494
51,929
(1,785)
30,595
17,858
99,185
(1,785)