

1 9 9 8   A N N U A L   R E P O R T

***DELPHI***  
Financial Group, Inc.

**Delphi Financial Group, Inc. is an integrated employee-benefit services company. It is a leader in managing all aspects of employee absence to enhance the productivity of its clients. It provides the related insurance coverages: short-term and long-term disability, primary and excess workers' compensation, group life, and travel accident, as well as underwriting and other services. Delphi's asset accumulation business emphasizes individual annuity products. Its common stock is listed on the New York Stock Exchange under the symbol DFG.**

### **1998 Highlights**

- Delphi earned after-tax operating income (excluding realized investment gains and losses) of \$81.8 million, up 25% from last year.
- A powerful distribution machine generated a 58% jump in new premium production.
- Delphi achieved a record \$87 million in net income, or \$4.13 per share, an increase of 16% over 1997's record results.
- Acquisitions completed in 1998 have transformed Delphi into a new kind of company—*an integrated employee-benefit services company*.
- Operating earnings per share reached \$3.88, a 22% increase over 1997.
- Delphi's stock appreciated 21% in 1998 compared with a rise of only 3% for the S&P Insurance Composite Index.

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*Over the past five years, we have, in fact, achieved a 38% compound annual growth rate in operating profits. This is one of the finest track records in our industry.*  
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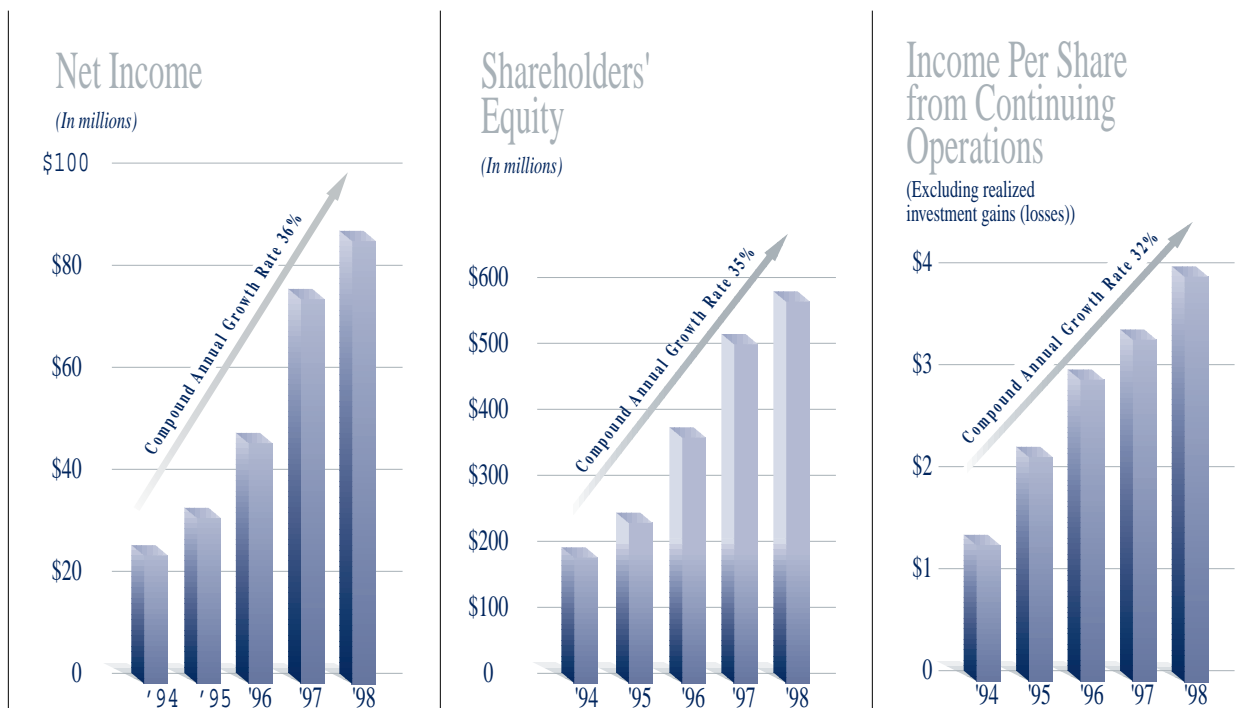
# Financial Highlights

## DELPHI FINANCIAL GROUP, INC.

(DOLLARS IN THOUSANDS, EXCEPT PER SHARE DATA)

Years Ended December 31,	1998	1997	1996	1995	1994
<b>Income Statement Data:</b>					
Insurance Premiums and Fee Income	\$ 449,884	\$ 360,871	\$ 335,233	\$ 260,902	\$ 248,512
Net Investment Income	168,692	162,380	157,020	117,112	106,576
Operating Profit	155,144	132,894	99,619	64,169	49,894
Operating Profit Excluding Realized Investment Gains (Losses)	147,084	118,326	102,270	63,465	39,681
Net Realized Investment Gains (Losses)	8,060	14,568	(2,651)	704	10,213
Income from Continuing Operations	87,035	74,982	53,854	32,742	25,944
Net Income	87,035	74,982	47,253	30,464	25,818
<b>Balance Sheet Data:</b>					
Total Assets	3,396,197	3,203,713	2,857,906	2,323,010	2,472,776
Long-Term Debt	265,165	178,769	231,004	134,611	159,577
Capital Securities of Delphi Funding L.L.C.	100,000	100,000	—	—	—
Shareholders' Equity	566,440	509,486	366,965	222,815	170,382
<b>Diluted Per Share Data*:</b>					
Income from Continuing Operations, Excluding Realized Investment Gains (Losses)	3.88	3.19	2.83	2.12	1.27
Income from Continuing Operations	4.13	3.65	2.75	2.15	1.71
Net Income	4.13	3.65	2.41	2.00	1.70
Book Value Per Share	27.66	25.06	18.14	14.61	11.21
Weighted Average Shares Outstanding (in thousands)	21,069	20,537	19,614	15,259	15,147

\* Prior period results per share and applicable share amounts have been restated to reflect stock dividends distributed in 1998.



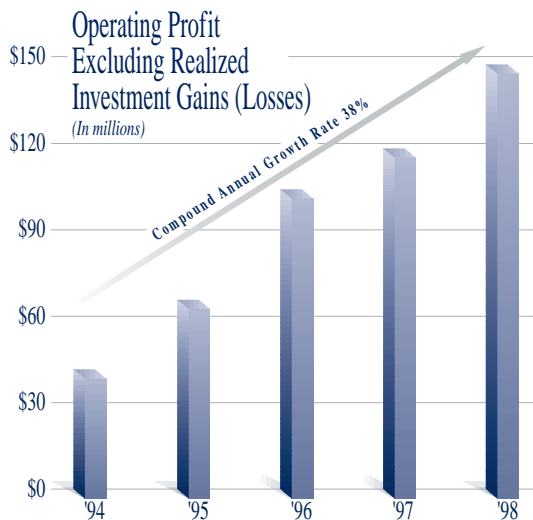
# Letter to Shareholders



**J**UST TAKE A LOOK AT DELPHI'S RESULTS FOR 1998—and you'll recognize at once a new, higher level of performance and profitability. Operating income for the full year climbed to a record \$81.8 million (or \$3.88 per share), 25% higher than a year ago. Realized capital gains boosted the year's total net income to \$4.13 per share, up 13% from a year ago—another record.

On the revenue line, premium income from our insurance operations was 29% higher in the fourth quarter of 1998 than in the same period of 1997, bringing 1998's total to \$418.4 million, up 17% from the year before. New premium production—a good indicator of what premium income will look like during the coming year, as new clients begin to pay their first full year's worth of premiums—was a remarkable 58% higher than in 1997.

In addition, we completed the acquisition of two subsidiaries in 1998, both of which are fee generating businesses that do not directly assume underwriting or investment risk. The first of these, Matrix Absence Management, Inc., is an important strategic addition to Delphi. Matrix is the leading provider of integrated disability services and provides real productivity enhancements to its large corporate clientele. The second is Uncover Managers, Inc., a manager of reinsurance pools, which provides an interesting counter-cyclical balance to our Safety National subsidiary.



We are confident that our excellent 1998 performance is a harbinger of things to come. We have generally exceeded our corporate goal of 15% earnings growth, and we have once again this year. Faster-growing earnings and a better strategic position—not a bad prospect for the future.

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# A New Kind of Company

The acquisitions we have made over the last three years have transformed Delphi. As we put the companies together and explored how they could work to enhance each other's activities, we discovered that the synergies were prodigious, sparking with energy.

Each of our companies, we found, boosted the horsepower of the others, so that the combination produced something closer to a geometrical rather than an arithmetical increase in total strength.

Most important of all, our companies dovetail perfectly to form one single, powerful totality—a new kind of company: we call it an

*integrated employee-benefit services company*. So far Delphi is unique in having created such a

company. It can provide the employers who are our clients a fully integrated array of services to

safeguard their employees—everything from short- and long-term disability insurance, to a complete

menu of workers' compensation insurance options, to productivity-boosting services to get high-value

employees back to work as quickly as possible after an injury. We can

already see that the uniqueness of our new strategic product mix

provides us with a significant competitive advantage, and it is just

beginning to provide us the kind of supercharged growth already

visible in the results reported above. It will produce advantages for

customers and shareholders alike.

*“As we put the companies together and explored how they could work to enhance each other's activities, we discovered that the synergies were prodigious, sparking with energy.”*

*“...our companies dovetail perfectly to form one single, powerful totality—a new kind of company: we call it an integrated employee-benefit services company.”*

How does the new company work? The best way to understand it is to look at how its constituent parts

came together to reinforce each other.

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## The Birth of Synergy

Start with Reliance Standard Life, our original operating subsidiary. Well-managed, highly-efficient, and long-established, it sells employers an array of employee-benefit group

*“...we have increased the production of new business since 1996 by 84%. In 1998, new production was up by 43% compared to the year before...”*

insurance: short- and long-term disability insurance, life and personal accident insurance. RSL has been traditionally notable for its skilled and disciplined underwriting—that is, the process by which it quite successfully chooses prospective new clients to make sure it excludes those likely to have higher-than-average disability claims. By rigidly managing its growth in this way, RSL has historically kept profits high

and has avoided the problems that have periodically buffeted some of its competitors.

But the real news in 1998 was the payoff from the investments we made over the last couple of years to greatly upgrade the quality of RSL's sales and marketing force. The productivity of the average salesperson has jumped by almost 40% over two years, so that with an increase from 46 to 61 marketing personnel, we have increased the production of new business since 1996 by 84%, without relaxing underwriting vigilance. In 1998, new production was up by 43% compared to the year before—a gratifying achievement.

These results have been achieved through the concerted efforts of RSL's management team in

*“These results have been achieved through the concerted efforts of RSL's management team in assembling a bigger and better marketing machine.”*

assembling a bigger and better marketing machine. In any insurance organization, control over effective and efficient distribution is a key ingredient for success. Operating from 21 strategically placed regional offices, we focus on and have developed important relationships with the full spectrum of brokers who advise and act on behalf of employers, the ultimate customers. Relationships with brokers, which are primarily local, are a key driver to new business generation and persistency. Of course, we need to offer attractive products at competitive prices. Building local broker confidence in our ability to deliver for his customer increases our chances of producing and maintaining business

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opportunities. Building a high level of confidence with the brokers takes years to develop and ultimately leads to a positive reputation. A lot of fundamental business practices go into this formula: responding as quickly as possible to brokers' inquiries and quotes; working with the broker to design products and terms that are responsive to his clients needs; treating claimants with the respect and fairness we all have come to expect—in a word, service. All of these factors help us differentiate ourselves in the market and have given us the ability to expand our franchise as quickly as we have in the past two years.

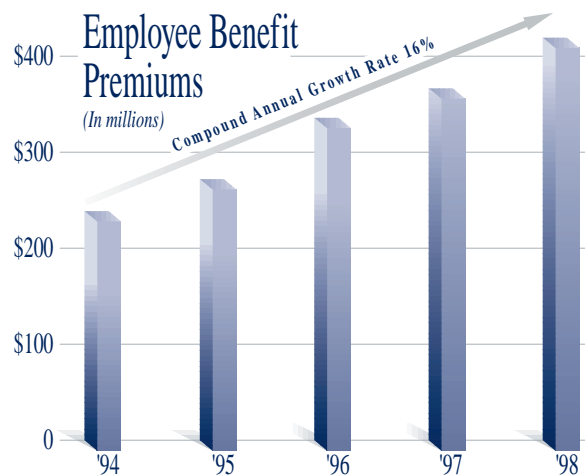
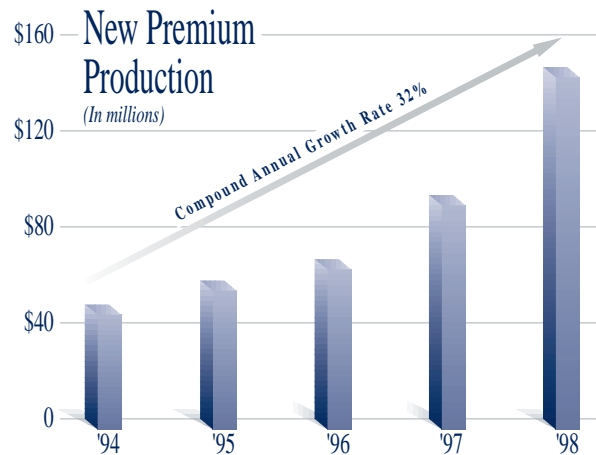
But, we are not sitting back on our laurels since the job never ends. We are currently producing business within RSL that, given our premium level and persistency, should sustain mid-teen top line growth. We have goals to improve persistency to further enhance future growth.

Our central focus, however, continues to be attracting a larger number of experienced marketing professionals to the team and expanding our new recruits into the business. More and better people should permit us to achieve our growth goals and enhance the productivity of the Company's marketing force.

Three years ago we made a major acquisition, Safety National Casualty Corporation, a market leader in the field of excess workers' compensation insurance. This sounds like an obscure product, but it is crucial to the success of the widespread movement to self-insure against workers' compensation risks.

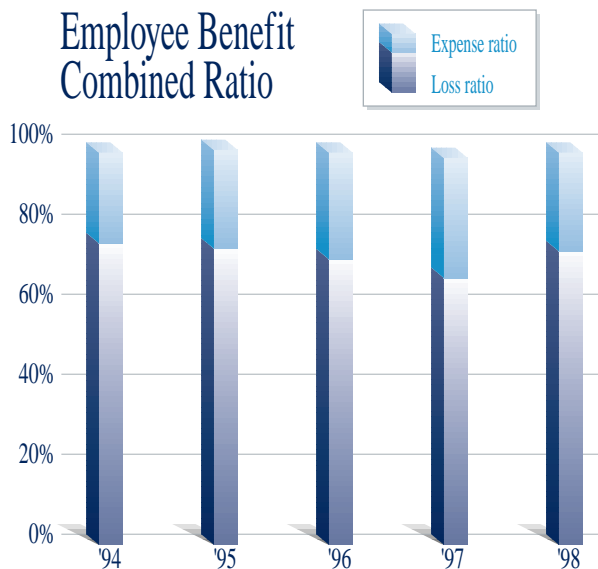
Workers' compensation is, of course, a giant business, since virtually all employers are required to provide this coverage; and a growing one as the dynamic U.S. economy continues to create private sector jobs.

Safety National's product works like this. Suppose an employer, or a consortium of employers, determines that it can save money by self-insuring against workers' compensation risks: by training and careful safety practices, it can keep claims low; by contracting out administration to an efficient supplier, it can keep overhead well below



that of the bloated, bureaucratic state insurance funds. The only cloud in this sunny picture is the prospect of some colossal, out of the ordinary claim, or a storm of normal ones, which could

## Employee Benefit Combined Ratio



drown a self-insurer's profits. Here is where Safety National comes in: companies that buy its coverage must pay out workers' compensation claims only up to a specified amount. Thereafter, Safety National pays the rest—the "excess" workers' compensation claims.

Safety National, when we bought it, had marketing representatives in only a handful of states, and that provided us with our first, modest foray into synergy. Since RSL is a truly national company, with coast-to-coast sales offices, we decided to station Safety National sales specialists in selected RSL regional offices, charged

with developing business among RSL's existing client base, who had, of course, a need for workers' compensation insurance as well as for RSL's products. We used RSL's distribution muscle to maintain Safety National's growth in a tough environment.

Excess workers' compensation is a cyclical business, and recently it has been in the gloomy seg-

*"...Safety National's revenues were up 14%. With entrepreneurial energy, it has begun to generate revenue from new sources..."*

ment of its cycle. That is because the rates for ordinary workers' compensation insurance—"first dollar coverage," as it is called—have been so low as to slow the trend toward self-insurance for the moment. It is a rare and fortunate feature of Safety National that its profits can keep growing, whether or not its premiums grow, because its clients pay in

premiums for many years before Safety National has to pay out any claims, and meanwhile it collects the investment income on those premiums. But even in this temporarily difficult environment, Safety National's revenues were up 14%. With entrepreneurial energy, it has begun to generate revenue from new sources, including first dollar workers' compensation coverage and loss portfolio transfers.

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## Matrix: A Strategic Keystone

Matrix Absence Management, Inc., acquired in June, is like the keystone in an arch that turns stacks of stones into a dynamic whole with the strength to support a vast and elaborate structure. Matrix, a leading provider of integrated disability services, provides corporate management two unique services. First, it takes over the responsibility of administering for them the complicated welter of programs dealing with employee absence and injury—everything from short- and long-term disability insurance and workers' compensation to the Family and Medical Leave Act and Social Security—all of which have different forms, eligibilities, and bureaucracies that are frustrating and confusing to navigate.

*“Matrix, a leading provider of integrated disability services, provides corporate management two unique services. First, it takes over the responsibility of administering for them the complicated welter of programs dealing with employee absence and injury...”*

Second, perhaps the most important part of Matrix's business is enhancing the productivity of its clients by making sure, whenever one of a client's highly skilled employees gets ill or injured, that he or she quickly receives the most advanced treatment or up-to-date rehabilitation from the appropriate specialists, in order to get back to work as soon as possible. Matrix helps employers install whatever special equipment might be necessary to get an injured employee back to work. Matrix's clients are concentrated in the fast-growing high-tech industry, rich in intellectual capital, and leaders in adopting “best practices” that soon spread to more-traditional firms. Matrix clients understand that they suffer real productivity losses when an employee gets sidelined: a single employee out for 20 days, according to one client estimate, can cost close to \$50,000 in lost productivity. This dwarfs the benefit costs that less astute employers focus upon.

*“Second, perhaps the most important part of Matrix's business is enhancing the productivity of its clients...”*

The strategic opportunity that Matrix offers to Delphi is enormous and exciting. When we bought it, Matrix was doing business mainly in California, where it had fully half of the Fortune 500 companies in the state as its clients. In fact, its client list is a Who's Who of the cutting-edge growth companies of the Information Age, including such gilt-edged technology pioneers as Intel, Netscape and Sun

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Microsystems. These clients were clamoring for Matrix's services in their non-California facilities, so our first order of business was to roll out Matrix nationwide. We started in 1998 by opening Matrix offices in such high-tech Meccas as Austin, Texas and commercially important areas such as Westchester, New York.

As we roll out Matrix across the country, think of the golden opportunities we create for the other parts of Delphi. Matrix clients are buyers of disability insurance, and Matrix can encourage them to consider RSL as their supplier. These are especially attractive clients for a disability insurer, for both the employer and the workforce share the ethic of doing whatever it takes to get the employee back to work quickly. As a result, there is a less-than-average likelihood of having injured employees linger on disability, avoiding costly consequences to the disability insurer.

*“Naturally, we have created an incentive structure that rewards employees of all of our companies handsomely for making these potentials for synergy a reality.”*

These are attractive prospects for RSL in another important respect. Hitherto, RSL's clients have been small- to medium-sized companies, appealing because they tend to be fast growing. But their relatively small size has this drawback: each piece of business RSL does with them is also relatively small, so it takes a lot of sales effort to build up to significant premium dol-

lars. Matrix's clients, by contrast, are large, premier corporations, so that every piece of business has several extra zeroes attached to it. Our Matrix acquisition, in other words, promises to expand RSL's market in an exceptionally advantageous way. It gives RSL access to the big leagues.

Matrix customers all provide workers' compensation coverage, as well. If they choose first dollar coverage, Safety National can provide it, either for its own account or as a fronting company. If they choose to self-insure, they can buy their excess workers' compensation insurance from Safety National. And if they choose to create a "captive reinsurer," the Delphi International connection comes into play. The pitch that Matrix can make to its clients is that, if they do business with Matrix's sister companies, they can choose whatever approach suits them best, and still depend on perfectly seamless coverage; there will be no squabbling between insurers about

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whether a given claim is a disability case or a workers' compensation case if the insurers are RSL and Safety National, with claims all administered by Matrix. Delphi can now provide all elements itself, very cost-effectively—something truly new and efficient in the marketplace. And some very significant Matrix clients have already bought into this proposition, even in the short time that we have had Matrix within the Delphi family. Naturally, we have created an incentive structure that rewards employees of all of our companies handsomely for making these potentials for synergy a reality. If the market should firm, Safety is well positioned to benefit.

## A Strategic Hedge

Our Unicover subsidiary, Delphi's most recent acquisition, and Safety National complement each other in an interesting way. To begin with, they are in niches of the workers' compensation business that are countercyclical to one another: in the climate that makes Safety National struggle hard for its growth, Unicover has flourished.

Unicover is a reinsurance-underwriting manager specializing in workers' compensation. Unicover is paid a fee for its services, primarily related to earned premiums. From a standing start just five years ago, Unicover now manages more than one billion dollars in premiums. This rapid growth was driven by Unicover's highly entrepreneurial corporate culture and its extraordinary technical expertise. It recognized that some large insurance companies, hungry for growth, were eager to participate in the giant workers' compensation market, but were not inclined to build up their own specialized operations in order to do so. Unicover provides the expertise to analyze and underwrite the workers' compensation risks, and to segment those risks into appropriate categories. It created and manages a "pool" and other facilities which earn premiums on behalf of the participating insurance companies. These are in turn protected by reinsurance coverage, or "retrocessionaires." The retrocessionaires, which are large, sophisticated, highly rated insurance companies, operating in a very soft reinsurance market, priced their layers of coverage aggressively. Unicover's pool and facilities have grown rapidly, in part by offering self-insured groups a "first dollar" alternative, and in part by reinsuring a select group of primary workers' compensation insurance companies.

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## A New Strategic Profile

In a nutshell, Delphi's new strategic profile looks like this: Reliance Standard Life has developed a highly efficient distribution machine. Its enhanced productivity has resulted in dramatic increases in new business production—up 84% since 1996; up 43% in 1998 alone. This distribution capacity has been marshaled to help maintain Safety National's growth in a tough environment. Uncover has added a hedge against the cyclicity of Safety National's business. Matrix, with its unique services in hot demand from big, blue-chip companies nationwide, not only can look forward to rapid and profitable expansion of its own services, but it can also take RSL's disability products into a new and lucrative market and can boost the sales and marketing of the workers' compensation products of Safety National. RSL's distribution strength is committed to the national roll-out of the Matrix service from its base in the high-tech companies of California. The fact that clients actively desire the seamless integration and comprehensiveness of the products and services Delphi now offers makes our new strategic interconnectedness an especially powerful competitive advantage to us. It is an exhilarating prospect for the future, and all parts of Delphi are fired up to make the whole bigger and stronger and even more profitable—by a large measure—than the sum of the parts.

## Investments

Delphi's investment yield for 1998 averaged 8.1%, compared to 7.9% the year before. In light of

*“Clearly, our effort over the last two years to make our investment results smoother and less volatile is succeeding.”*

the extraordinary volatility in the financial markets in 1998, we view these results as entirely satisfactory and an eloquent testimony to our success in managing our investment operations so as to minimize volatility. Clearly, our effort over the last two years to make our investment results smoother and less volatile is succeeding.

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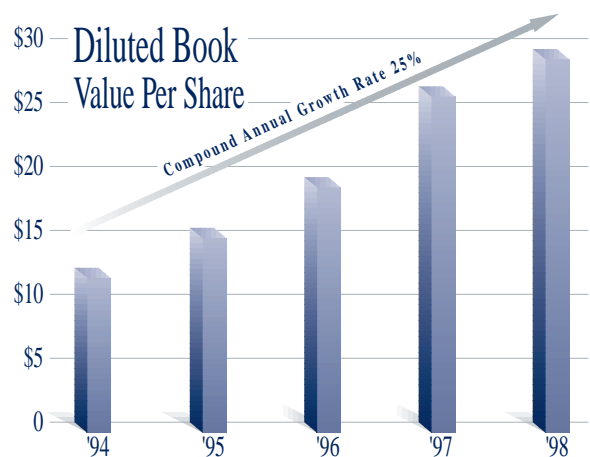
We realized \$.25 per share of capital gains during 1998, which reflects Delphi's continual effort to be responsive to investment conditions in redeploying its portfolio. As rates fell early in the year, we were able to take gains in certain portions of the portfolio and to redeploy those assets advantageously. Later in the year, when interest spreads widened, portions of the portfolio that were more sensitive to these and other market conditions underperformed, so we took the opportunity to take some losses and reposition the portfolio favorably in the year's second half.

## Summary

Delphi has generally exceeded its corporate goals to earn 15% on its equity, and to grow earnings at a 15% rate. Over the past five years, we have, in fact, achieved a 38% compound annual growth rate in operating profits. This is one of the finest track records in our industry. And more important than any of the numbers is our extraordinary strategic position: a unique provider of integrated employee-benefit services, with clear, large scale profit opportunities as our business units work together.

We are proud to have created a new kind of company, an *integrated employee-benefit services company*. As investors appreciate the strategic value of what we have built, we believe they will accord Delphi a pre-

mium multiple, reflecting its superior historic performance and future prospects. We are particularly pleased that in 1998 Delphi delivered to its shareholders returns that were way in excess of insurance indices, especially for companies of comparable size. Delphi stock appreciated 21% during the year compared with a rise of 3% for the S&P Insurance Composite Index.



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Since year-end, Unicover has been subject to adverse publicity due to possible reserve strengthening by one major retrocessionaire of its managed reinsurance pools. Unicover does not assume insurance risk in its role as manager of reinsurance pools. Moreover, Unicover is a separate legal entity and it is solely responsible for its own liabilities. Therefore, we do not believe that Unicover issues will have a material impact on us. Delphi's risk, if any, is strictly limited to its small investment in this company. We have used the opportunity presented by a market drop in our stock price to accelerate our existing one million share buyback program, as we are confident in our future prospects.

1999 should be another rewarding year for our shareholders, as we enjoy the benefits of the strategic repositioning we have achieved and as the market becomes aware of the changes that have transformed Delphi.

Respectfully submitted,

A handwritten signature in black ink, appearing to read "Robert Rosenkranz", with a stylized flourish at the end.

Robert Rosenkranz  
Chairman of the Board

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## Board of Directors

**Robert Rosenkranz**

*Chairman of the Board, President  
and Chief Executive Officer*

**Edward A. Fox**

*Chairman of the Board  
SLM Holdings, Inc.*

**Charles P. O'Brien**

*President and Chief Executive Officer  
Reliance Standard Life Insurance Company*

**Lewis S. Ranieri**

*Chairman and Chief Executive Officer  
Ranieri & Co., Inc.*

**Thomas L. Rhodes**

*President and Director  
National Review, Inc.*

**Robert M. Smith, Jr.**

*Vice President  
Delphi Financial Group, Inc.*

**B. K. Werner**

*Chairman Emeritus  
Safety National Casualty Corporation*

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## Corporate Information

**Corporate Headquarters**

1105 North Market Street, Suite 1230  
P.O. Box 8985  
Wilmington, DE 19899  
(302) 478-5142 • (302) 427-7663 Fax

**Annual Meeting**

Tuesday, May 11, 1999, at 10:00<sup>AM</sup>  
University Club  
One West 54th Street  
New York, NY 10019

**Investor Relations**

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c/o 2501 Parkway  
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(215) 787-3943 • (215) 787-3944 Fax  
E-mail: invrel@dlfi.com

**Registrar and Stock Transfer Agent**

First Union National Bank  
Corporate Trust Department - 1153  
1525 West W.T. Harris Boulevard, 3C3  
Charlotte, NC 28288-1153  
(800) 829-8432

**Trading Market**

New York Stock Exchange  
Symbol: DFG

**Independent Accountants**

Ernst & Young LLP  
Two Commerce Square, Suite 4000  
2001 Market Street  
Philadelphia, PA 19103

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## Principal Subsidiaries

**Delphi Capital Management, Inc.**

153 East 53rd Street  
New York, NY 10022  
(212) 838-7000 • (212) 838-7598 Fax • DLPHI@dlfi.com

**Reliance Standard Life Insurance Company**

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**Unicover Managers, Inc.**

One Cragwood Road  
South Plainfield, NJ 07080  
(908) 668-4596 • (908) 668-0805 Fax

**Safety National Casualty Corporation**

2043 Woodland Parkway  
St. Louis, MO 63146  
(314) 995-5300 • (314) 995-3843 Fax • SNCC@sncc.com

**Matrix Absence Management, Inc.**

2099 Gateway Place  
San Jose, CA 95110  
(408) 453-7700 • (408) 453-9977 Fax • Webmaster@matrixcos.com

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## Principal Officers

**Delphi Financial Group, Inc.**

Robert Rosenkranz  
*Chairman of the Board, President  
and Chief Executive Officer*

Chad W. Coulter  
*Vice President and General Counsel*

Lawrence E. Daurelle  
*Vice President and Treasurer*

Linda Eike  
*Secretary*

Louis C. Lucido  
*Vice President, Investments*

Robert M. Smith, Jr.  
*Vice President*

**Reliance Standard Life  
Insurance Company**

Charles P. O'Brien  
*President and Chief Executive Officer*

David R. Armstrong  
*Vice President, Group Underwriting*

Chad W. Coulter  
*Vice President, General Counsel  
and Assistant Secretary*

Lawrence E. Daurelle  
*Vice President and Treasurer*

Charles T. Denaro  
*Secretary*

Christopher A. Fazzini  
*Vice President, Sales and Marketing*

Kenneth R. Hamm  
*Vice President, Strategic Planning*

Debra G. Staples  
*Vice President, Claims Administration*

**Safety National  
Casualty Corporation**

B. K. Werner  
*Chairman Emeritus*

Harold F. Ilg  
*Chairman of the Board*

Terence T. Schoeninger  
*President and Chief Executive Officer*

John P. Csik  
*Vice President of Finance,  
Assistant Treasurer*

Duane A. Hercules  
*Executive Vice President and Treasurer*

Eugene R. Maier  
*Vice President of Underwriting*

Jeffrey W. Otto  
*Secretary and General Counsel*

Stuart M. Presson  
*Senior Vice President of Marketing*

Gerald R. Scott  
*Executive Vice President,  
Assistant Secretary*

Mark A. Wilhelm  
*Executive Vice President*

**Matrix Absence  
Management, Inc.**

David F. Nolan  
*Chairman and Chief Executive Officer*

Martin Grable  
*President and Chief Operating Officer*

**Unicover Managers, Inc.**

John E. Pallat, III  
*Chairman and Chief Executive Officer*

Kenneth C. Griebell  
*Vice President*

***DELPHI***

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