

Edgar Filing: DEFENSE INDUSTRIES INTERNATIONAL INC - Form 10QSB

DEFENSE INDUSTRIES INTERNATIONAL INC  
Form 10QSB  
May 20, 2003

U.S. SECURITIES AND EXCHANGE COMMISSION  
Washington, D.C. 20549

FORM 10-QSB

X Quarterly report under Section 13 or 15(d) of the Securities Exchange Act of 1934 for the quarterly period ended March 31, 2003

\_\_\_ Transition report under Section 13 or 15(d) of the Exchange Act for the transition period from \_\_\_ to \_\_\_

Commission file number: 1-9009

Defense Industries International, Inc.  
(Exact Name of Small Business Issuer as Specified in Its Charter)

Nevada  
(State of Incorporation)

84-1421483  
(I.R.S. Employer Identification No.)

Industrial Zone Erez, P.O. Box 779, Ashkelon 78101, Israel  
(Address of Principal Executive Offices)

(011) 972-7-689-1611  
(Issuer's Telephone Number, Including Area Code)

\_\_\_\_\_  
(Former Name, Former Address and Former Fiscal Year,  
if Changed Since Last Report)

Check whether the issuer: (1) filed all reports required to be filed by Section 13 or 15(d) of the Exchange Act during the past 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 CORPORATE ISSUERS

As of May 19, 2003 the Issuer had 25,350,000 shares of Common Stock, no par value per share, outstanding.

Transitional Small Business Disclosure Format (check one):

Yes \_\_\_ No X

DEFENSE INDUSTRIES INTERNATIONAL, INC.  
(FORMERLY PAWNBROKERS EXCHANGE, INC.) AND SUBSIDIARIES

INDEX

Part I - Financial Information:

## Edgar Filing: DEFENSE INDUSTRIES INTERNATIONAL INC - Form 10QSB

- Item 1. Condensed Consolidated Balance Sheets - March 31, 2003  
(Unaudited) and December 31, 2002
- Condensed Consolidated Statements of Income and Comprehensive Income  
for the Three Months Ended March 31, 2003 and 2002 (Unaudited)
- Condensed Consolidated Statements of Cash Flows  
For the Three Months Ended March 31, 2003 and  
2002 (Unaudited)
- Notes to the Condensed Consolidated Financial Statements -  
(Unaudited) 6
- Item 2 Management's Discussion and Analysis of  
Financial Condition and Results of Operations
- Item 3. Controls and Procedures
- Part II - Other Information:
- Item 4. Submission of Matters to a Vote of Shareholders
- Item 6. Exhibits and Reports on Form 8-K
- Signatures

### PART I - FINANCIAL INFORMATION

Item 1.

DEFENSE INDUSTRIES INTERNATIONAL, INC.  
(FORMERLY PAWNBROKERS EXCHANGE, INC.) AND SUBSIDIARIES

Condensed Consolidated Balance Sheets

	March 31, 2003 (Unaudited)	December -----
ASSETS		
CURRENT ASSETS		
Cash and cash equivalents	\$1,026,911	
Trade accounts receivable, net	2,634,287	
Trade accounts receivable - related parties, net	183,646	
Shareholder note receivable	277,474	
Other receivables	362,212	
Inventories	1,827,092	
Deferred taxes	85,373	
	-----	
Total current assets	6,396,995	
	-----	
PROPERTY, PLANT AND EQUIPMENT, NET	1,826,723	

Edgar Filing: DEFENSE INDUSTRIES INTERNATIONAL INC - Form 10QSB

OTHER ASSETS	
Investment in marketable securities	496,857
Deposits for the severance of employer-employee relations	427,233
Deferred taxes, long-term	238,519
Intangible assets	45,604
	-----
Total other assets	1,208,213
	-----
TOTAL ASSETS	\$9,431,931
	=====

See accompanying notes to condensed consolidated financial statements.

1

PART I - FINANCIAL INFORMATION

DEFENSE INDUSTRIES INTERNATIONAL, INC.  
(FORMERLY PAWNBROKERS EXCHANGE, INC.) AND SUBSIDIARIES

Condensed Consolidated Balance Sheets (Cont.)

March 31, 2003  
(Unaudited)

LIABILITIES AND SHAREHOLDERS' EQUITY	
CURRENT LIABILITIES	
Short-term bank credit	\$724,330
Trade accounts payable	1,010,197
Current portion of long-term debt	333,362
Other liabilities	1,224,886
	-----
Total current liabilities	3,292,775
	-----
LONG TERM LIABILITIES	
Long-term loans	772,824
Provision for the severance of employer- employee relations	435,296
Minority interest	830,092
	-----
Total long-term liabilities	2,038,212
	-----
TOTAL LIABILITIES	5,330,987
	-----
COMMITMENTS AND CONTINGENCIES	
SHAREHOLDERS' EQUITY	
Preferred stock, \$.0001 par value, 50,000,000 shares authorized, none issued and outstanding	-
Common stock, \$.0001 par value, 250,000,000	

Edgar Filing: DEFENSE INDUSTRIES INTERNATIONAL INC - Form 10QSB

shares authorized, 25,550,000 and 25,400,000 issued and outstanding, respectively	2,525
Common stock to be issued (250,000 shares)	10
Additional paid-in capital	1,711,450
Retained earnings	2,814,121
Accumulated other comprehensive loss	(427,162)
Deferred consulting fees	-
	-----
Total shareholders' equity	4,100,944
	-----
 TOTAL LIABILITIES AND SHAREHOLDERS' EQUITY	 \$9,431,931
	=====

See accompanying notes to condensed consolidated financial statements.

2

DEFENSE INDUSTRIES INTERNATIONAL, INC.  
(FORMERLY PAWNBROKERS EXCHANGE, INC.) AND SUBSIDIARIES

Condensed Consolidated Statements of Income and Comprehensive Income  
(Unaudited)

	Three Months Ended
	-----
	2003
	-----
REVENUES	\$3,168,144
Cost of sales and processing	2,273,812
	-----
Gross profit	894,332
	-----
OPERATING EXPENSES	
Selling	188,676
General and administrative	323,348
	-----
TOTAL OPERATING EXPENSES	512,024
	-----
INCOME FROM OPERATIONS	382,308
	-----
OTHER INCOME (EXPENSE)	
Interest, dividends and gain (loss) on sales of securities, net	(70,753)
Other income - net	-
	-----
TOTAL OTHER INCOME (EXPENSE)	(70,753)
	-----

Edgar Filing: DEFENSE INDUSTRIES INTERNATIONAL INC - Form 10QSB

INCOME BEFORE INCOME TAXES	311,555
Income tax expense	129,247
	-----
INCOME BEFORE MINORITY INTEREST	182,308
Minority interest	8,196
	-----
NET INCOME	\$174,112
	-----
OTHER COMPREHENSIVE INCOME (LOSS)	
Foreign currency translation gain (loss), net of minority interest translation loss	37,858
Unrealized gain (loss) on available-for-sale securities	(3,202)
	-----
Other comprehensive income (loss) before tax	34,656
Income tax (expense) benefit related to items of other comprehensive income	(12,476)
	-----
TOTAL OTHER COMPREHENSIVE INCOME (LOSS), NET OF TAX	22,180
	-----
COMPREHENSIVE INCOME	\$196,292
	=====
Net income per share - basic and diluted	\$0.01
	=====
Weighted average number of shares outstanding during the period - basic and diluted	25,350,000
	=====

See accompanying notes to condensed consolidated financial statements.

3

DEFENSE INDUSTRIES INTERNATIONAL, INC.  
(FORMERLY PAWNBROKERS EXCHANGE, INC.) AND SUBSIDIARIES

Condensed Consolidated Statements of Cash Flows  
(Unaudited)

	For the Three Months Ended	
	2003	(
	-----	-----
CASH FLOWS FROM OPERATING ACTIVITIES:		
Net Income	\$ 174,111	\$
Adjustments to reconcile net income to net cash used in operating activities:		
Depreciation and amortization	70,032	
Stock issued for services	43,000	
Minority interest in income of subsidiary	8,196	
Changes in operating assets and liabilities:		
Decrease (increase) in deposits for employee		

Edgar Filing: DEFENSE INDUSTRIES INTERNATIONAL INC - Form 10QSB

severance	(12,883)
Decrease (increase) in deferred taxes	1,104
Decrease (increase) in trade accounts receivable	(642,850)
Decrease (increase) in other receivable	(175,344)
Decrease (increase) in inventory	(92,126)
Increase (decrease) in trade accounts payable	27,396
Increase (decrease) in other liabilities	476,698
Increase (decrease) in provision for employee severance	37,360
	-----
Net Cash Used In Operating Activities	(85,306)
	-----
CASH FLOWS FROM INVESTING ACTIVITIES:	
Purchase of property and equipment	(42,132)
Proceeds from sale of property and equipment	-
Repayments received on shareholders loans	103,512
Investment in marketable securities	(146,011)
Proceeds from sale of marketable securities	134,156
	-----
Net Cash Provided By (Used In) Investing Activities	49,525
	-----

See accompanying notes to condensed consolidated financial statements.

4

DEFENSE INDUSTRIES INTERNATIONAL, INC.  
(FORMERLY PAWNBROKERS EXCHANGE, INC.) AND SUBSIDIARIES  
Condensed Consolidated Statements of Cash Flows (Cont.)  
(Unaudited)

	For the Three Months 2003
CASH FLOWS FROM FINANCING ACTIVITIES:	
	-----
Short-term bank credit, net	298,332
Payments on long term debt	(91,698)
Loan payable - related party	-
	-----
Net Cash Provided By (Used In) Financing Activities	206,634
	-----
Effect of exchange rate changes on cash	24,238
	-----
NET INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS	195,091
CASH AND CASH EQUIVALENTS - BEGINNING OF PERIOD	831,820
	-----
CASH AND CASH EQUIVALENTS - END OF PERIOD	\$1,026,911
	=====

# Edgar Filing: DEFENSE INDUSTRIES INTERNATIONAL INC - Form 10QSB

INTEREST PAID	\$58,584
TAXES PAID	\$41,968

See accompanying notes to condensed consolidated financial statements.

5

## DEFENSE INDUSTRIES INTERNATIONAL, INC. (FORMERLY PAWNBROKERS EXCHANGE, INC.) AND SUBSIDIARIES

### Notes to Condensed Consolidated Financial Statements (Unaudited)

#### NOTE 1 BASIS OF PRESENTATION AND SIGNIFICANT ACCOUNTING POLICIES

##### (A) Basis of Presentation

The accompanying condensed consolidated financial statements are presented in United States dollars under accounting principles generally accepted in the United States.

##### (B) Principles of Consolidation

The condensed consolidated financial statements for 2003 include the accounts of Defense Industries International, Inc. , formerly Pawnbrokers Exchange, Inc. ("PEI"), and its wholly owned subsidiaries, Export Erez, USA, Inc., Export Erez, Ltd., Mayotex, Ltd. and Dragonwear Trading Ltd., and its 76% owned subsidiary Achidatex Nazareth Elite (1977) Ltd. (collectively, the "Company"). The minority interest represents the minority shareholders' proportionate share of Achidatex.

Effective March 25, 2002, PEI began doing business as Defense Industries International, Inc. On July 8, 2002, PEI changed its corporate domicile from Utah to Nevada (the "re-incorporation"). In order to accomplish the re-incorporation, PEI merged with and into its wholly owned subsidiary, Defense Industries International, Inc., a Nevada corporation. As a result, PEI's name was changed from PEI to Defense Industries International, Inc. Each issued and outstanding share of PEI capital stock on the effective date was converted into and exchanged for one share of Defense Industries capital stock. Defense Industries is authorized to issue 250,000,000 shares of \$.0001 par value common stock and 50,000,000 shares of \$.0001 par value preferred stock.

All intercompany accounts and transactions have been eliminated in consolidation.

##### (C) Use of Estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States requires management to make estimates and assumptions that effect the reported amounts of assets and liabilities and disclose the nature of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting periods. Actual results could differ from those estimates.

DEFENSE INDUSTRIES INTERNATIONAL, INC.  
(FORMERLY PAWNBROKERS EXCHANGE, INC.) AND SUBSIDIARIES

Notes to Condensed Consolidated Financial Statements  
(Unaudited)

(D) Per Share Data

Basic net income per common share is computed based on the weighted average common shares outstanding during the year. Diluted net income per common share is computed based on the weighted average common shares and common stock equivalents outstanding during the year. The computation of weighted average common shares outstanding gives retroactive effect to the recapitalization discussed in Note 4. There were no common stock equivalents outstanding because the exercise price of the common stock equivalents exceeded the average market price of the stock. Accordingly, a reconciliation between basic and diluted earnings per share is not presented.

(E) Interim Consolidated Financial Statements

The condensed consolidated financial statements as of March 31, 2003 and for the three months ended March 31, 2003 and 2002 are unaudited. In the opinion of management, such condensed consolidated financial statements include all adjustments (consisting only of normal recurring accruals) necessary for the fair presentation of the consolidated financial position and the consolidated results of operations. The condensed consolidated results of operations for the three months ended March 31, 2003 are not necessarily indicative of the results to be expected for the full year. The condensed consolidated balance sheet information as of December 31, 2002 was derived from the audited consolidated financial statements included in the Company's Annual Report on Form 10-KSB. The interim condensed consolidated financial statements should be read in conjunction with that report.

(F) Reclassifications

Certain prior period amounts have been reclassified to conform to the current period presentation.

(G) Prior Period Adjustment

The accompanying condensed consolidated statement of income for the three months ended March 31, 2002 has been restated to correct an error for the understatement of depreciation expense as previously reported in the Company's March 31, 2002 10-QSB filing. The effect of the restatement was to decrease net income by \$36,000. There was no effect on earnings per share.

DEFENSE INDUSTRIES INTERNATIONAL, INC.  
(FORMERLY PAWNBROKERS EXCHANGE, INC.) AND SUBSIDIARIES

Notes to Condensed Consolidated Financial Statements  
(Unaudited)

NOTE 2 INVENTORY

## Edgar Filing: DEFENSE INDUSTRIES INTERNATIONAL INC - Form 10QSB

Inventory consisted of the following:

	March 31, 2003	December 31, 2002
Raw materials	\$1,349,405	
Work in process	320,713	
Finished goods	\$156,974	
	=====	
	\$1,827,092	
	=====	

### NOTE 3 SHAREHOLDER NOTE RECEIVABLE

On January 15, 2002, the Company loaned \$400,000 to an officer who is also its controlling shareholder. The note was for a term of eleven months and matured on December 15, 2002, bore interest of 8% and required quarterly prepaid interest payments only. At March 31, 2003, the note receivable remained outstanding and had a balance of \$277,474. The officer plans to settle the note in 2003 by: (1) paying \$77,474; and (2) delivering 327,869 shares of the Company's common stock held by the officer valued at \$200,000. The failure to satisfy the note at maturity may be deemed to be a violation of the newly enacted Sarbanes Oxley Act of 2002. As indicated above, the Company intends to resolve this matter during 2003. Uncertainty exists as to the ultimate resolution of the matter and whether such resolution will have a material impact on the Company's consolidated financial position and the results of operations. No accruals with respect to this note have been made in the accompanying consolidated balance sheets at March 31, 2003.

### NOTE 4 SHAREHOLDERS' EQUITY

On March 25, 2002, PEI, a reporting public company with no assets, liabilities or operations, consummated a share exchange agreement (the "Agreement") with Export Erez USA, Inc., ("Export USA") a Delaware corporation, whereby all of the shares of Export USA were converted into 21,000,000 shares, or 84%, of the common stock of PEI.

Under generally accepted accounting principles, a company whose shareholders receive over fifty percent of the stock of the surviving entity in a business combination is considered the acquirer for accounting purposes. Accordingly, the transaction was accounted for as an acquisition of PEI and a recapitalization of Export USA. The consolidated financial statements subsequent to the acquisition include the following: (1) the balance sheet consists of the net assets of PEI at historical costs (zero at the acquisition date) and the net assets of Export USA and subsidiaries at historical cost; and (2) the statement of operations consists of the operations of Export USA and subsidiaries for the period presented and the operations of PEI from the recapitalization date.

On April 8, 2002, the Company entered into a one-year agreement with a consultant whereby the Company issued 100,000 shares of its common stock in return for future consulting services. The 100,000 shares were valued at \$172,000, the fair market value of the common stock on the grant date based on the prevailing market price. Consulting expense of \$43,000 was recognized for the quarter ended March 31, 2003.

On July 30, 2002, the Company entered into a one-year agreement with a consultant whereby the Company agreed to issue 700,000 shares of common stock in return for future consulting services. The contract was terminated after one month, and the Company, in accordance with the settlement reached with the consultant, issued 150,000 common shares on February 1, 2003. The 150,000 shares were valued at \$334,475, the fair market value of the common stock on the grant date based on the prevailing market price. The

## Edgar Filing: DEFENSE INDUSTRIES INTERNATIONAL INC - Form 10QSB

consulting expense was recognized during the fourth quarter of 2002.

8

DEFENSE INDUSTRIES INTERNATIONAL, INC.  
(FORMERLY PAWNBROKERS EXCHANGE, INC.) AND SUBSIDIARIES

Notes to Condensed Consolidated Financial Statements  
(Unaudited)

NOTE 5 SEGMENT INFORMATION

The Company has two strategic business units: the civilian market and the military market. The military market is further broken down between local and export sales in order to better analyze trends in sales and profit margins. The Company does not allocate assets between segments because several assets are used in more than one segment and any allocation would be impractical.

	Civilian	Local	Military Local	Military Export
	-----		-----	-----
March 31, 2003				
Revenues	\$	421,532	\$	998,747
Income from operations		73,316		97,562
March 31, 2002				
Revenues	\$	977,613	\$	1,386,809
Income from operations (as restated)		346,771		250,708

NOTE 6 SUBSEQUENT EVENT

On November 29, 2001, the Company entered into a one-year agreement with a consultant whereby the consultant agreed to assist the Company in having its securities gain listing on a stock exchange, to raise capital and to settle disputes the Company had against other companies. In return, the agreement required the Company to issue 10,000 shares of the Company's common stock monthly and to reimburse the consultant for out-of-pocket expenses. In the event the consultant was successful in settling disputes, the consultant was entitled to receive additional equity compensation. A dispute with respect to the agreement with the consultant arose in 2002. A settlement was signed on May 1, 2003 and the Company has accrued an aggregate amount of \$111,069 under the agreement.

9

ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

THE FOLLOWING IS MANAGEMENT'S DISCUSSION AND ANALYSIS OF CERTAIN SIGNIFICANT FACTORS WHICH HAVE AFFECTED OUR FINANCIAL POSITION AND OPERATING RESULTS DURING THE PERIODS INCLUDED IN THE ACCOMPANYING CONDENSED CONSOLIDATED FINANCIAL STATEMENTS. THE DISCUSSION AND ANALYSIS WHICH FOLLOWS MAY CONTAIN TREND ANALYSIS AND OTHER FORWARD-LOOKING STATEMENTS WITHIN THE MEANING OF SECTION 21E OF THE SECURITIES EXCHANGE ACT OF 1934 WHICH REFLECT OUR CURRENT VIEWS WITH RESPECT TO FUTURE EVENTS AND FINANCIAL RESULTS. THESE INCLUDE STATEMENTS REGARDING OUR EARNINGS, PROJECTED GROWTH AND FORECASTS, AND SIMILAR MATTERS THAT ARE NOT HISTORICAL FACTS. WE REMIND SHAREHOLDERS THAT FORWARD-LOOKING STATEMENTS ARE MERELY PREDICTIONS AND THEREFORE ARE INHERENTLY

## Edgar Filing: DEFENSE INDUSTRIES INTERNATIONAL INC - Form 10QSB

SUBJECT TO UNCERTAINTIES AND OTHER FACTORS THAT COULD CAUSE THE FUTURE RESULTS TO DIFFER MATERIALLY FROM THOSE DESCRIBED IN THE FORWARD-LOOKING STATEMENTS.

### CRITICAL ACCOUNTING POLICIES

We have identified the following policies as critical to the understanding of our financial statements. The preparation of our financial statements requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of sales and expenses during the reporting periods. Areas where significant judgments are made include, but are not limited to, inventory valuation and revenue recognition. Actual results could differ materially from these estimates. Our consolidated financial statements have been prepared in accordance with accounting principles generally accepted in the United States.

**REVENUES AND REVENUE RECOGNITION.** Revenues from sales of products are recognized under the completed contract method upon shipment to customers. The contracts are short term, generally under two months. We provide a warranty on goods ranging from three to four years. Our policy is to consider the establishment of a reserve for warranty expenses. Based upon historical experience of no warranty claims, we have not established a reserve at December 31, 2002 and March 31, 2003.

**INVENTORIES.** Inventories are stated at the lower of cost or market. Cost is determined by the moving average method, inventories write-offs and write-down provisions are provided to cover risks arising from slow-moving items or technological obsolescence.

**FOREIGN CURRENCY TRANSLATION AND TRANSACTIONS.** The functional currency of Export Erez, Ltd., Mayotex Ltd., and Achidatex Nazareth Elite is the New Israeli Shekel (NIS). The functional currency of Dragonwear Trading Ltd. is the Cyprus Pound (CYP). The financial statements of Dragonwear are translated into NIS. The financial statements for all of these entities are then translated into United States dollars from NIS at quarter-end exchange rates as to assets and liabilities and weighted average exchange rates as to revenues and expenses. Capital accounts are translated at their historical exchange rates when the capital transactions occurred. Foreign currency transaction gains or losses from transactions denominated in currencies other than NIS are recognized in net income in the period the gain or loss occurs.

10

**COMPREHENSIVE INCOME (LOSS).** Foreign currency translation gains (losses) resulting from the translation of the financial statements of our company and its subsidiaries expressed in NIS to United States dollars are reported as Other Comprehensive Income (Loss) in the Statement of Income and as Accumulated Other Comprehensive Income (Loss) in the Statement of Shareholders' Equity. The unrealized gains and losses, net of tax, resulting from the valuation of available-for-sale securities at their fair market value at period end are reported as Other Comprehensive Income (Loss) in the Statement of Income and as Accumulated Other Comprehensive Income (Loss) in the Statement of Shareholders' Equity.

**INVENTORIES.** Inventories are valued at the lower of cost or market value using the first-in first-out method for raw materials. The cost includes expenses of freight-in transportation. The specific identification method is used for finished goods since all orders are custom orders for customers.

**PROPERTY AND EQUIPMENT.** Fixed assets are stated at cost less accumulated depreciation. Depreciation is computed using the straight-line method over the

## Edgar Filing: DEFENSE INDUSTRIES INTERNATIONAL INC - Form 10QSB

estimated useful lives of three to twenty-five years. These long-lived assets are generally evaluated on an individual basis in making a determination as to whether such assets are impaired. Periodically, we review our long-lived assets for impairment based on estimated future non discounted cash flows attributed to the assets. In the event such cash flows are not expected to be sufficient to recover the recorded value of the assets, the assets are written down to their estimated fair values.

**INCOME TAXES.** Deferred tax assets and liabilities are recognized for the future tax consequences attributable to differences between the financial statement carrying amounts of existing assets and liabilities and their respective tax bases. Deferred tax assets and liabilities are measured using enacted tax rates expected to apply to taxable income in the years in which those temporary differences are expected to be recovered or settled. The effect on deferred tax assets and liabilities of a change in tax rates is recognized in income in the period that includes the enactment date.

### OVERVIEW

Defense Industries International, Inc. is a manufacturer and global provider of personal military and civilian protective equipment and supplies. Our products are used by military, law enforcement, border patrol enforcement, and other special security forces, corporations, non-governmental organizations and individuals throughout the world.

Our main products include body armor, bomb disposal suits and bullet proof vests and jackets, ballistic wall covers helmets, plates, and one-way protective windows, personal military equipment, battle pouch units and combat harness units, dry storage units, liquid logistics, tents and vehicle covers, winter suits, sleeping bags and backpacks.

Our strategic objective is to be a leading global provider of personal military and civilian protective equipment and supplies. We intend to realize our strategic objective through the following:

11

- o **PURSUE STRATEGIC ACQUISITIONS.** We intend to selectively pursue acquisitions that enhance our product lines and geographic presence in an effort to consolidate our highly fragmented industry and to create a more diverse and global reach for us in our marketplace.
- o **FOCUS ON INTERNAL GROWTH.** We intend to focus on the internal expansion of our existing businesses, thereby placing us in a position to offer a more comprehensive portfolio of products to satisfy all of our customers' protective equipment needs.
- o **CAPITALIZE ON INCREASED DEMAND FOR OUR PRODUCTS.** As a result of the terrorist attacks on September 11, 2001, and other recent world events, an increased emphasis on safety and protection now exists worldwide. This has translated into increased spending on personal, military and civilian protective equipment and supplies. We expect a continued increase in volume for our current major government programs and expect to participate in other existing and future government programs that require our products. We also expect a continued increase in sales to the growing civilian market.
- o **EXPAND MARKETING EFFORTS** In the wake of the terrorist attacks of September 11, 2001, and other recent world events, a greater global recognition regarding the need for our products has materialized. We intend to capitalize on this increased interest in our products by broadening our marketing efforts in an attempt to create better global brand and

## Edgar Filing: DEFENSE INDUSTRIES INTERNATIONAL INC - Form 10QSB

recognition awareness of us and our products.

- o EXPAND DISTRIBUTION NETWORK AND PRODUCT OFFERINGS. We intend to widen our distribution network through strategic acquisitions and the development of new products. We believe that a broader product line will enable us to both strengthen our relationships with existing customers and attract new customers.

THREE MONTHS ENDED MARCH 31, 2003 COMPARED WITH THREE MONTHS ENDED MARCH 31, 2002

### RESULTS OF OPERATIONS

SALES AND GROSS PROFIT MARGIN. Sales for the three months ended March 31, 2003 were \$3,168,144 compared to \$2,621,220 for the same period in 2002. This increase in sales resulted from a 580.6% increase in export sales. The increase in export sales from \$256,798 for the three months ended March 31, 2002 to \$1,747,865 in the 2003 period was due to the successful implementation of our growth plan. Specifically, we believe that the increase is the result of the successful implementation of our marketing efforts to create a better global brand and gain worldwide recognition of our company as well as for our products. We believe that the decrease in sales to our local market (see below) is due to the recession in Israel. We do not expect that our sales in Israel will increase until the government implements a new economic plan and not before the third quarter of 2003 at the earliest. The breakdown of sales for the three months ended March 31, 2003 and 2002 is as follows:

12

	2003		2002
	----		----
Sales to the local civilian market	\$ 421,532	\$	977,613
Sales to the local military market	998,747		1,386,809
Export military sales	1,747,865		256,798

Gross profit for the three months ended March 31, 2003 was \$894,332 compared to \$1,017,391 for the same period in 2002. This decrease in gross profit is primarily attributable to increased overseas sales which are not as profitable as local sales due to higher costs. We believe that the level of profit from future export sales will be higher, as a result of change in the composition of the products to be exported.

Gross profit margin for the three months ended March 31, 2003 was 28.2% compared to 38.8% for the same period in 2002. Our gross profit margin on our increased overseas sales is lower than on local sales due to higher costs. We believe that the level of profit from future export sales will be higher, as a result of change in the composition of the products to be exported.

The cost of production for the three months ended March 31, 2003 was \$2,273,812 compared to \$1,603,829 for the same the same period in 2002. This increase is a result of increased overseas sales as well as a 21% overall increase in sales.

GENERAL AND ADMINISTRATIVE EXPENSES AND SELLING EXPENSES. General and administrative costs for three months ended March 31, 2003 were \$323,348 compared to \$266,017 for the same period in 2002. This increase is due to

## Edgar Filing: DEFENSE INDUSTRIES INTERNATIONAL INC - Form 10QSB

increased professional expenditures, such as legal fees advertising, consultants and market analysts. These expenditures arose from the increased costs associated with becoming a publicly traded company on a U.S. securities market and from our efforts to achieve public awareness of our company and products in North America. Selling expenses for the three months ended March 31, 2003 were \$188,676 compared to \$94,667 for the same period in 2002. This increase is a result of commissions arising from the increase in overseas sales.

**INCOME TAX EXPENSES.** Income tax expense for the three months ended March 31, 2003 was \$129,247 as compared to \$222,193 for the comparable period in 2002. Our effective tax rate was 41% in the 2003 period compared to 36% in 2002. The increase in the effective tax rate is primarily attributable to the utilization of net operations loss carryforwards in 2002 that have expired in 2003.

**OTHER INCOME (EXPENSE), NET.** Other income (expense), net for the three months ended March 31, 2003 was (\$70,753) as compared to (\$32,146) for the same period in 2002. Our financing expenditures increased as a result of the devaluation of the shekel against the dollar and the increase in interest payments on our short term bank debt.

**MINORITY INTEREST.** For the three months ended March 31, 2003 we recognized and recorded minority interest of \$8,196 compared to \$23,086 for the same period in 2002.

**NET INCOME.** As a result of the foregoing our net income for the three months ended March 31, 2003 was \$174,112 compared to \$379,282 for the 2002 period.

13

### LIQUIDITY AND CAPITAL RESOURCES

As of March 31, 2003, we had \$1,026,911 in cash and cash equivalents and our working capital was \$3,104,220. Our current activities are financed by short and long term bank loans offset by short term deposits. Our decision to incur additional short term debt was based on our consideration of the prevailing yields on our deposits which are generally in foreign currency generated from receipts from overseas sales, compared to the cost of short term loans. Our long term loans arose from acquisition of Achidatex and are payable over five years.

Net cash used in operating activities was \$85,306 for the three months March 31, 2003. This amount was primarily attributable to a \$476,698 increase in other liabilities and our net income of \$174,112 offset by a \$642,850 increase in trade accounts receivable, and a \$175,344 increase in other receivables and a \$92,126 increase in inventory.

The increase in accounts receivable at March 31, 2003 compared to year end was primarily the result of the increased level of sales in the first quarter of 2003. Similarly, the increase in inventory for the three months ended March 31, 2003 was primarily due to our increased level of operations.

Net cash provided by investing activities was \$49,525 for the three months ended March 31, 2003. During the three months ended March 31, 2003, \$146,011 of cash was used for investments in marketable securities and \$42,132 was used for purchases of property and equipment offset by \$103,512 generated from repayments recovered on the shareholders loan.

We anticipate increasing our research and development expenditures in 2003 and 2004, primarily with respect to ballistic helmets, stab-resistant fabric, ceramic ballistic plates, ballistic wall covering and one-way protective windows. We anticipate total research and development expenses for 2003 and 2004

## Edgar Filing: DEFENSE INDUSTRIES INTERNATIONAL INC - Form 10QSB

will be approximately \$350,000 and \$750,000 respectively. The development of these products will be by staff engineers. We expect that production of these products will start by the end of 2003, increasing to full production by the year 2006. We anticipate that in order to fund the research and development for these products, we may seek to raise capital by means of an offering of our equity securities. If we are unable to effect an offering of our securities, we may fund our research and development expenditures through our operating funds. In such event, the timing of our anticipated research and development and subsequent production schedule would be delayed.

We believe that sufficient funds to fund our operations during the remainder of 2003.

### MARKET RISK

At March 31, 2003 and December 31, 2002, we held cash and cash equivalents in the aggregate amount of \$1,026,911 and \$831,820, respectively, most of these amounts were deposited with Israeli banks. Under Israeli law, the Bank of Israel insures all bank deposits without limits on the amount. Therefore, we do not anticipate losses in respect to these items.

14

The majority of our sales are made to government institutions and private industry in Israel. Consequently, the exposure to credit risks relating to trade receivables is limited. We perform ongoing credit evaluations of our customers and generally do not require collateral. An appropriate allowance for doubtful accounts is included in trade accounts receivable.

### ITEM 3. CONTROLS AND PROCEDURES

Within the 90 days prior to the date of the filing of this Form 10-QSB, we carried out an evaluation, under the supervision and with the participation of our management, including our chief executive officer and chief financial officer, of the effectiveness of the design and operation of our disclosure controls and procedures pursuant to Rule 13a-14 of the Securities Exchange Act of 1934. Based upon that evaluation, our chief executive officer and chief financial officer concluded that our disclosure controls and procedures are effective in timely alerting them to material information relating to us required to be included in our periodic SEC filings. There have been no significant changes in our internal controls or other factors which could significantly affect internal controls subsequent to the date we carried out its evaluation.

We also maintains a system of internal accounting controls that is designed to provide assurance that our assets are safeguarded and that transactions are executed in accordance with management's authorization and properly recorded. This system is continually reviewed and is augmented by written policies and procedures, the careful selection and training of qualified personnel and an internal audit program to monitor its effectiveness. During the quarter ended March 31, 2003, there were no significant changes to this system of internal controls or in other factors that could significantly affect those controls.

15

## PART II - OTHER INFORMATION

DEFENSE INDUSTRIES INTERNATIONAL, INC. AND SUBSIDIARIES

Edgar Filing: DEFENSE INDUSTRIES INTERNATIONAL INC - Form 10QSB

ITEM 4. SUBMISSION OF MATTERS TO A VOTE OF SHAREHOLDERS

None.

ITEM 6. EXHIBITS AND REPORTS ON FORM 8-K

(A) EXHIBITS

99.1 Certification by Chief Executive Officer Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.

99.2 Certification by Chief Financial Officer Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.

99.3 Certification by Chief Executive Officer Pursuant to 18 U.S.C. Section 1350, As Adopted Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.

99.4 Certification by Chief Financial Officer Pursuant to 18 U.S.C. Section 1350, As Adopted Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.

(B) Reports on Form 8-K:

16

SIGNATURES

Pursuant to the requirements of Section 13 or 15(d) 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.

DEFENSE INDUSTRIES INTERNATIONAL, INC.  
(Registrant)

Name: Joseph Postbinder  
Chief Executive Officer

Name: Tsippy Moldovan  
Chief Financial Officer

17

EXHIBIT 99.1

CERTIFICATION PURSUANT TO SECTION 302(A)  
OF THE SARBANES-OXLEY ACT OF 2002

I, Joseph Postbinder, certify that:

1. I have reviewed this quarterly report on Form 10-QSB of Defense Industries International, Inc.;
2. Based on my knowledge, this quarterly report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such

## Edgar Filing: DEFENSE INDUSTRIES INTERNATIONAL INC - Form 10QSB

statements were made, not misleading with respect to the period covered by this quarterly report;

3. Based on my knowledge, the financial statements, and other financial information included in this quarterly report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this quarterly report;
4. The registrant's other certifying officers and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-14 and 15d-14) for the registrant and we have:
  - a) designed such disclosure controls and procedures to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this quarterly report is being prepared;
  - b) evaluated the effectiveness of the registrant's disclosure controls and procedures as of a date within 90 days prior to the filing date of this quarterly report (the "Evaluation Date"); and
  - c) presented in this quarterly report our conclusions about the effectiveness of the disclosure controls and procedures based on our evaluation as of the Evaluation Date;
5. The registrant's other certifying officers and I have disclosed, based on our most recent evaluation, to the registrant's auditors and the audit committee of registrant's board of directors (or persons performing the equivalent function):
  - a) all significant deficiencies in the design or operation of internal controls which could adversely affect the registrant's ability to record, process, summarize and report financial data and have identified for the registrant's auditors any material weaknesses in internal controls; and
  - b) any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal controls; and
6. The registrant's other certifying officers and I have indicated in this quarterly report whether or not there were significant changes in internal controls or in other factors that could significantly affect internal controls subsequent to the date of our most recent evaluation, including any corrective actions with regard to significant deficiencies and material weaknesses.

May 20 , 2003

---

Joseph Postbinder

Chief Executive Officer

EXHIBIT 99.2

CERTIFICATION PURSUANT TO SECTION 302(A)

Edgar Filing: DEFENSE INDUSTRIES INTERNATIONAL INC - Form 10QSB

OF THE SARBANES-OXLEY ACT OF 2002 I,

I, Tsippy Moldovan, certify that:

1. I have reviewed this quarterly report on Form 10-QSB of Defense Industries International, Inc.;
2. Based on my knowledge, this quarterly report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this quarterly report;
3. Based on my knowledge, the financial statements, and other financial information included in this quarterly report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this quarterly report;
4. The registrant's other certifying officers and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-14 and 15d-14) for the registrant and we have:
  - a) designed such disclosure controls and procedures to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this quarterly report is being prepared;
  - b) evaluated the effectiveness of the registrant's disclosure controls and procedures as of a date within 90 days prior to the filing date of this quarterly report (the "Evaluation Date"); and
  - c) presented in this quarterly report our conclusions about the effectiveness of the disclosure controls and procedures based on our evaluation as of the Evaluation Date;
5. The registrant's other certifying officers and I have disclosed, based on our most recent evaluation, to the registrant's auditors and the audit committee of registrant's board of directors (or persons performing the equivalent function):
  - a) all significant deficiencies in the design or operation of internal controls which could adversely affect the registrant's ability to record, process, summarize and report financial data and have identified for the registrant's auditors any material weaknesses in internal controls; and b) any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal controls; and
6. The registrant's other certifying officers and I have indicated in this quarterly report whether or not there were significant changes in internal controls or in other factors that could significantly affect internal controls subsequent to the date of our most recent evaluation, including any corrective actions with regard to significant deficiencies and material weaknesses.

May 20 , 2003

---

Edgar Filing: DEFENSE INDUSTRIES INTERNATIONAL INC - Form 10QSB

Tsippy Moldovan

Chief Financial Officer

EXHIBIT 99.3

CERTIFICATION PURSUANT TO 18 U.S.C. SECTION 1350  
AS ADOPTED PURSUANT TO SECTION 906  
OF THE SARBANES-OXLEY ACT OF 2002

In connection with the Quarterly Report of Defense Industries International, Inc. (the "Company") on Form 10-QSB for the period ending March 31, 2003 as filed with the Securities and Exchange Commission on the date hereof (the "Report"), I, Joseph Postbinder, Chief Executive Officer of the Company, certify, pursuant to 18 U.S.C. ss. 1350, as adopted pursuant to ss. 906 of the Sarbanes-Oxley Act of 2002, that:

- (1) The Report fully complies with the requirements of section 13(a) or 15(d) of the Securities Exchange Act of 1934; and
- (2) The information contained in the Report fairly presents, in all material respects, the financial condition and result of operations of the Company.

---

Joseph Postbinder  
Chief Executive Officer  
May 20 , 2003

EXHIBIT 99.4

CERTIFICATION PURSUANT TO 18 U.S.C. SECTION 1350  
AS ADOPTED PURSUANT TO SECTION 906  
OF THE SARBANES-OXLEY ACT OF 2002

In connection with the Quarterly Report of Defense Industries International, Inc. (the "Company") on Form 10-QSB for the period ending March 31, 2003 as filed with the Securities and Exchange Commission on the date hereof (the "Report"), I, Tsippy Moldovan, Chief Financial Officer of the Company, certify, pursuant to 18 U.S.C. ss. 1350, as adopted pursuant to ss. 906 of the Sarbanes-Oxley Act of 2002, that:

- (1) The Report fully complies with the requirements of section 13(a) or 15(d) of the Securities Exchange Act of 1934; and
- (2) The information contained in the Report fairly presents, in all material respects, the financial condition and result of operations of the Company.

---

Tsippy Moldovan  
Chief Financial Officer  
May 20 , 2003