DEFENSE INDUSTRIES INTERNATIONAL INC
Form 10QSB
August 14, 2002

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

FORM 10-QSB

(X) QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

( ) TRANSACTION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For Quarter Ended: June 30, 2002 Commission File Number: 000-30105

DEFENSE INDUSTRIES INTERNATIONAL, INC.

(Exact name of Registrant as specified in its charter)

NEVADA	84-1421481
(State or other jurisdiction of incorporation or organization)	(IRS Employer Identification Number)

Industrial Zone Erez
P.O. Box 779
Ashkelon, Israel 78101

(Address of Principal Executive Offices) (Zip Code)

011-972-8-689-1611

(Registrant's telephone number, including area code)

Indicate by check mark whether the 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 filing requirements for the past 90 days.

Yes X No___

The number of shares of Common Stock, no par value per share, outstanding as of June 30, 2002 is 25,400,000.

Transitional Small Business Disclosure Format (check one): Yes__ No X

PART I - FINANCIAL INFORMATION

ITEM 1. FINANCIAL STATEMENTS

DEFENSE INDUSTRIES INTERNATIONAL, INC.
(FORMERLY PAWNBROKERS EXCHANGE, INC.)
AND SUBSIDIARIES
CONDENSED CONSOLIDATED
FINANCIAL STATEMENTS
AS OF JUNE 30, 2002

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

CONTENTS

DEFENSE INDUSTRIES INTERNATIONAL, INC.
(FORMERLY PAWNBROKERS EXCHANGE, INC.) AND SUBSIDIARIES
CONDENSED CONSOLIDATED BALANCE SHEETS

ASSETS

		June 30, 2002 (Unaudited)		December 31, 2001 (As Restated)
CURRENT ASSETS				
Cash and cash equivalents	$	540,054	$	781,996
Trade accounts receivable, net		1,692,195		2,461,671
Trade accounts receivable - related parties, net		140,728		181,059
Shareholder note receivable		400,000		-
Other receivables and debit balances		410,610		274,840
Inventories		1,945,054		1,956,072
Deferred taxes		105,219		97,761
Total Current Assets		5,233,860		5,753,399
PROPERTY, PLANT AND EQUIPMENT, NET		1,826,348		1,951,147
OTHER ASSETS				
Investment in marketable securities		521,526		616,105
Deposits for the severance of employer-employee relations		384,536		472,421
Deferred taxes, long-term		278,847		400,689
Intangible assets		52,099		61,452
Total Other Assets		1,237,008		1,550,667
Total assets	$	8,297,216	$	9,255,213

DEFENSE INDUSTRIES INTERNATIONAL, INC.
(FORMERLY PAWNBROKERS EXCHANGE, INC.) AND SUBSIDIARIES
CONDENSED CONSOLIDATED BALANCE SHEETS

LIABILITIES AND SHAREHOLDERS' EQUITY

	June 30, 2002 (Unaudited)	December 31, 2001 (As Restated)

CURRENT LIABILITIES		
Short-term bank credit	$ 693,560	$ 894,981
Trade accounts payable	1,092,729	1,551,470
Current portion of long-term debt	349,525	371,344
Other accounts payable and credit balances	963,307	1,011,062
Total Current Liabilities	3,099,121	3,828,857
LONG-TERM LIABILITIES		
Long-term loans	650,045	1,295,440
Long-term loan - related party	-	47,432
Provision for the severance of employer-employee relations	418,884	431,522
Minority interest	600,445	572,106
Total Long-Term Liabilities	1,669,374	2,346,500
Total liabilities	4,768,495	6,175,357
COMMITMENTS AND CONTINGENCIES		
SHAREHOLDERS' EQUITY		
Common stock, no par value, 300,000,000 shares authorized, 25,400,000 and 21,000,000 issued and outstanding, respectively	2,069,485	1,147,485
Retained earnings	3,018,499	2,396,616
Accumulated other comprehensive loss	(680,263)	(464,245)
Deferred consulting fees	(879,000)	-
Total Shareholders' Equity	3,528,721	3,079,856
Total liabilities and shareholders' equity	$ 8,297,216	$ 9,255,213

DEFENSE INDUSTRIES INTERNATIONAL, INC.
(FORMERLY PAWNBROKERS EXCHANGE, INC.) AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENTS OF INCOME AND
COMPREHENSIVE INCOME (LOSS)
(UNAUDITED)

	For the Three Months	For the Three Months	For the Six Months	For the Six Months

	Ended June 30, 2002	Ended June 30, 2001	Ended June 30, 2002	Ended June 30, 2001
REVENUES	$ 2,692,415	$ 942,188	$ 5,313,635	$ 2,039,258
Cost of sales and processing	1,663,279	616,126	3,267,108	1,373,989
Gross profit	1,029,136	326,062	2,046,527	665,269
OPERATING EXPENSES				
Selling expenses	228,016	40,292	322,683	101,897
General and administrative expenses	333,121	182,296	599,165	264,568
TOTAL OPERATING EXPENSES	561,137	222,588	921,848	366,465
INCOME FROM OPERATIONS	467,999	103,474	1,124,679	298,804
OTHER INCOME (EXPENSE)				
Financial income (expense), net	(33,144)	(41,012)	(66,295)	(30,046)
Other income - net	11,915	31,116	12,920	49,028
TOTAL OTHER INCOME (EXPENSE)	(21,229)	(9,896)	(53,375)	18,982
INCOME BEFORE INCOME TAXES	446,770	93,578	1,071,304	317,786
Income tax expense	185,888	14,766	408,081	97,743
INCOME BEFORE MINORITY INTEREST	260,882	78,812	663,223	220,043
Minority interest	(18,254)	(7,313)	(41,340)	(7,313)
NET INCOME	$ 242,628	$ 71,499	$ 621,883	$ 212,730
OTHER COMPREHENSIVE INCOME (LOSS)				
Foreign currency translation gain (loss), net of minority interest translation loss	10,272	15,702	(163,128)	(58,142)
Unrealized gain (loss) on available-for-sale securities	(61,260)	31,023	(52,890)	(93,982)
Other comprehensive income (loss) before tax	(50,988)	46,725	(216,018)	(152,124)
Income tax (expense) benefit related to items of other comprehensive income	18,356	(16,821)	77,766	54,765
TOTAL OTHER COMPREHENSIVE INCOME (LOSS), NET OF TAX	(32,632)	29,904	(138,252)	(97,359)
COMPREHENSIVE INCOME (LOSS)	$ 209,996	$ 101,403	$ 483,631	$ 115,371

Net income per ordinary share - basic and diluted	$ 0.01	$ 0.00	$ 0.03	$ 0.01
Weighted average number of shares outstanding during the period - basic and diluted	25,149,171	20,099,993	23,314,917	20,025,407

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DEFENSE INDUSTRIES INTERNATIONAL, INC.
(FORMERLY PAWNBROKERS EXCHANGE, INC.) AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENT OF CHANGES IN SHAREHOLDERS' EQUITY
FOR THE SIX MONTHS ENDED JUNE 30, 2002
(UNAUDITED)

	Common Stock Shares	Amount	Retained Earnings	Deferred Fees	A C In
Balance, January 1, 2002 (as previously reported)	21,000,000	$ 1,147,485	$ 2,468,669	$ -	
Prior period adjustment - error in depreciation expense	-	-	(72,053)	-	
Balance, January 1, 2002 (as restated)	21,000,000	1,147,485	2,396,616	-	
Common stock transferred in recapitalization	4,000,000	-	-	-	
Common stock issued for services	400,000	922,000	-	(879,000)	
Foreign currency translation loss	-	-	-	-	
Unrealized loss on available for sale securities	-	-	-	-	
Net income 2002	-	-	621,883	-	
BALANCE, JUNE 30, 2002	25,400,000	$ 2,069,485	$ 3,018,499	$ (879,000)	

DEFENSE INDUSTRIES INTERNATIONAL, INC.
(FORMERLY PAWNBROKERS EXCHANGE, INC.) AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS
(UNAUDITED)

	For The Six Months Ended June 30, 2002	For The Six Months Ended June 30, 2001
CASH FLOWS FROM OPERATING ACTIVITIES:		
Net Income	$ 621,883	$ 212,730
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization	140,983	55,431
Stock issued for services	43,000	-
Minority interest in income of subsidiary	28,339	-
Gain from sale of fixed assets	-	(15,377)
Decrease (increase) in deposits for employee severance	87,885	1,426
Decrease (increase) in deferred taxes	114,384	221
Decrease (increase) in trade accounts receivable	809,806	(337,345)
Decrease (increase) in other receivables and debit balances	(135,769)	4,486
Decrease (increase) in inventory	11,018	22,860
Increase (decrease) in trade accounts payable	(458,741)	(51,457)
Increase (decrease) in other accounts payable and credit balances	(47,755)	109,082
Increase (decrease) in provision for employee severance	(12,638)	7,676
Net Cash Provided By Operating Activities	1,202,395	9,733
CASH FLOWS FROM INVESTING ACTIVITIES:		
Purchase of property and equipment	(58,312)	(60,927)
Proceeds from sale of property and equipment	3,167	17,392
Investment in marketable securities	(17,421)	(18,397)
Cash acquired in acquisition of Achidatex	-	39,147
Funds advanced on behalf of shareholder	(400,000)	-
Advances related to acquisition, net	-	56,820
Loan to subsidiary	-	(480,000)
Net Cash Used in Investing Activities	(472,566)	(445,965)
CASH FLOWS FROM FINANCING ACTIVITIES:		
Short-term bank credit, net	(201,421)	515,141
Payments on long term debt	(667,214)	(10,885)
Loan payable - related party	(47,432)	-
Net Cash Provided By (Used In) Financing Activities	(916,067)	504,256
Effect of exchange rate changes on cash	(55,704)	(33,315)

Net increase (decrease) in cash and cash equivalents	(241,942)	34,709
Cash and cash equivalents - beginning of period	781,996	663,295
Cash and cash equivalents - end of period	$ 540,054	$ 698,004
INTEREST PAID	$ 69,546	$ 43,665
TAXES PAID	$ 59,521	$ 59,407

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DEFENSE INDUSTRIES INTERNATIONAL, INC.
(FORMERLY PAWNBROKERS EXCHANGE, INC.) AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS
(UNAUDITED)

SUPPLEMENTAL DISCLOSURE OF NON-CASH INVESTING ACTIVITIES:

On March 25, 2002, the Company issued 21,000,000 shares of common stock to acquire Export Erez USA, Inc.

On April 8, 2002, the Company issued 100,000 shares of common stock for consulting services aggregating $172,000 of which $43,000 has been expensed and $129,000 has been deferred at June 30, 2002.

On April 30, 2002, the Company issued 300,000 shares of common stock under a consulting agreement valued at $750,000. No consulting services have been performed to date in connection with this agreement and the entire amount has been deferred.

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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 of America.

(B) Principles of Consolidation

The condensed consolidated financial statements for 2002 include the accounts of Defense Industries International, Inc. (formerly Pawnbrokers Exchange, Inc. (see Note 7)) 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 (collectively, the "Company"). The minority interest represents the minority shareholders' proportionate share of Achidatex.

The consolidated financial statements for 2001 include the accounts of Export Erez, USA, Inc. and its wholly owned subsidiaries, Export Erez, Ltd., Mayotex, Ltd. and Dragonwear Trading Ltd. and its 76% owned subsidiary Achidatex Nazareth Elite from June 18, 2001, the date of acquisition (See Note 5).

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 of America 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.

(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.

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(E) Interim Consolidated Financial Statements

The condensed consolidated financial statements as of June 30, 2002 and for the three and six months ended June 30, 2002 and 2001 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 consolidated results of operations for the three and six months ended June 30, 2002 and 2001 are not necessarily indicative of the results to be expected for the full year.

The condensed consolidated balance sheet information as of December 31, 2001 was derived from the audited consolidated financial statements included in the Company's annual report Form 10-KSB. The interim condensed consolidated financial statements should be read in conjunction with that report.

(F) Prior Period Adjustment

The accompanying condensed consolidated balance sheet as of December 31, 2001 has been restated to correct an error for the understatement of depreciation expense during 2001. The effect of the restatement was to decrease net income for 2001 by $72,053. Retained earnings and property, plant and equipment, net in the December 31, 2001 consolidated balance sheet and retained earnings in the consolidated statement of changes in shareholders' equity have been restated for the effects of the prior period adjustment.

NOTE 2 INVENTORY

Inventory consisted of the following:

	June 30, 2002	December 31, 2001
Raw materials	$ 1,325,855	$ 1,166,086
Work in process	276,717	491,237
Finished goods	342,481	298,749
	$ 1,945,054	$ 1,956,072

NOTE 3 SHAREHOLDER LOAN RECEIVABLE

On January 15, 2002, the Company loaned $400,000 to the Company's controlling shareholder. The note is for a term of eleven months maturing December 15, 2002, bears interest of 8% and requires quarterly prepaid interest payments only. Interest on this loan was not paid until August 2002 and approximately $10,000 of interest income has been accrued for the period ended June 30, 2002.

NOTE 4 SHAREHOLDERS' EQUITY

(A) Recapitalization

On March 25, 2002, Pawnbrokers Exchange, Inc. ("PEI"), a reporting public company with no assets, liabilities or operations at that time, consummated a share exchange agreement (the "Agreement") with Export Erez USA, Inc., ("Export USA") a company incorporated in Delaware whereby all of the shareholders in Export USA had their shares converted into 21,000,000 shares or 84% of the common stock of PEI.

Under generally accepted accounting principles, a company whose stockholders 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 the Company and a recapitalization of Export USA. The condensed consolidated financial statements subsequent to the acquisition include the following: (1) the balance sheet consists of the net assets of the Company at historical costs (zero at the acquisition date) and the net assets of Export USA at historical cost. (2) the statement of operations consists of the operations of Export USA for the period presented and the operations of the Company from the recapitalization date.

As a result of the recapitalization, $1,146,169 was reclassified from additional paid-in capital to common stock in the accompanying June 30, 2002 balance sheet. For comparative purposes, $1,146,169 was reclassified from additional paid-in capital to common stock in the accompanying December 31, 2001 balance sheet in order to conform to the June 30, 2002 presentation.

(B) Issuances of Common Stock

On April 8, 2002, the Company entered into a one-year agreement with a consultant whereby the Company issued 100,000 shares of 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 as of June 30, 2002 and $129,000 is reflected as a deferred consulting expense component of equity.

On April 30, 2002, the Company entered into a one-year agreement with a consultant whereby the Company issued 300,000 shares of common stock in return for future consulting services. The 300,000 shares were valued at $750,000 the fair market value of the common stock on the grant date based on the prevailing market price. The contract is in dispute and no services have been performed to date. Counsel for the Company is confident that the Company will prevail and receive its 300,000 shares back. Therefore, no consulting expense was recognized as of June 30, 2002 and $750,000 is reflected as a deferred consulting expense component of equity.

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DEFENSE INDUSTRIES INTERNATIONAL, INC.
(FORMERLY PAWNBROKERS EXCHANGE, INC.) AND SUBSIDIARIES
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(UNAUDITED)

NOTE 5 BUSINESS COMBINATION

Effective June 18, 2001, the Company acquired 76% of the total common stock of Achidatex Nazareth Elite (1977) Ltd. ("Achidatex"). Accordingly, the results of operations of Achidatex are included in the condensed consolidated financial statements for the six months ended June 30, 2002.

For comparative purposes, following are the summarized unaudited pro forma condensed consolidated results of operations for the six months ended June 30, 2001, assuming the acquisition had taken place at the beginning of 2001. The unaudited pro forma results are not necessarily indicative of future earnings or earnings that would have been reported had the acquisition been completed when assumed.

Net revenues	$ 5,157,674
Income before income taxes	$ 683,574
Income tax expense (benefit)	$ (607,530)
Minority interest, net of tax	$ 264,368
Net income	$ 1,026,736
Net income per share	$ 0.05

NOTE 6 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	Consolidated
June 30, 2002				
Net Sales	$ 2,011,659	$ 2,506,343	$ 795,633	$ 5,313,635
Income from operations	560,312	392,739	171,628	1,124,679
June 30, 2001				
Net Sales	$ 960,620	$ 804,102	$ 274,536	$ 2,039,258
Income from operations	177,604	94,086	27,114	298,804

NOTE 7 SUBSEQUENT EVENT

Effective July 8, 2002, the Company changed its corporate domicile from the State of Utah to the State of Nevada (the "re-incorporation"). In order to accomplish the re-incorporation, the Company merged with and into its wholly-owned subsidiary, Defense Industries International, Inc., a Nevada corporation. As a result of the re-incorporation, the Company's name was effectively changed from Pawnbrokers Exchange, Inc. to Defense Industries International, Inc. Each share of Pawnbrokers capital stock issued and outstanding 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.

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

Cautionary Statement Pursuant to Safe Harbor Provisions of the Private Securities Litigation Reform Act of 1995:

This Quarterly Report on Form 10-QSB for the quarterly period ended June 30, 2002 contains "forward-looking" statements within the meaning of Section 27A of the Securities Act of 1933, as amended, including statements that include the words "believes", "expects", "anticipates", or similar expressions. These forward-looking statements may include, among others, statements of expectations, beliefs, future plans and strategies, anticipated events or trends, and similar expressions concerning matters that are not historical facts. The forward-looking statements in this Quarterly Report on Form 10-QSB for the quarterly period ended June 30, 2002 involve known and unknown risks, uncertainties and other factors that could the cause actual results, performance or achievements of the Company to differ materially from those expressed in or implied by the forward-looking statements contained herein.

OVERVIEW

The strategic objective of Defense Industries International, Inc. is to be the leading global provider of personal military and civilian protective equipment and supplies. We intend to realize our strategic objective through the following:

-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 our company in the marketplace.

-Focus on Internal Growth: We intend to focus on internal expansion of our businesses, thereby placing our company in a position to offer an even more comprehensive portfolio of products to satisfy all of our customers' protective equipment needs.

-Capitalize On Increased Demand for Company 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 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 for our products.

-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 recognition awareness of our company and our products.

-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 strengthen our relationship with existing customers and attract new customers at the same time.

RESULTS OF OPERATIONS

Three Months Ended June 30, 2002 Compared to Three Months Ended June 30,2001

SALES AND GROSS PROFIT MARGIN

Sales in the three months ended June 30, 2002 increased to $2,692,415 or 185.8% from $942,188 for the same three months in 2001. We attribute this increase in sales to the acquisition of Achidatex, Ltd. in June 2001, and the increased demand for our products. The breakdown of sales for the three months ended June 30 is as follows:

	2002 ($)	2001 ($)
Sales to the local market-civilian	1,034,046	474,474
Sales to the local market-military	1,119,535	287,481
Export sales-military	538,835	180,233
Totals $	2,692,416	942,188

Gross profit for the three months ended June 30, 2002 increased to $1,029,136 or 215.7% from $326,062 for the same three months in 2001. This increase in gross profit is explained partly by the acquisition of Achidatex, Ltd. in June 2001, and the increased demand for our products. The gross margin for the three months ended June 30, 2002 improved to 38% as compared to 34.6% for the same three months in 2001.

The cost of production for the three months ended June 30, 2002 was $1,663,279 compared to $616,126 for the same three months in 2001. This change in cost of production is explained partly by the acquisition of Achidatex, Ltd..

GENERAL AND ADMINISTRATIVE EXPENSES

General and administrative costs in the three months ended June 30, 2002 were $333,121 compared to $182,296 for the same three months in 2001. This change is explained partly by the acquisition of Achidatex, Ltd.

INCOME TAX EXPENSE

Income tax expense for the three months ended June 30, 2002 was $185,888 or 41.6% of income before income taxes, as compared to $14,766 or 15.8% of income before income taxes for the three months ended June 30,2001.

The effective income tax rate increased in 2002 as compared to 2001 as a result of several factors. Certain stock-based non-cash operating expenses incurred in 2002 at the US holding company level were not deductible against the income generated at the Israel subsidiaries for income tax purposes. In addition, depreciation expense with respect to fixed assets of approximately $1,441,000 acquired in conjunction with the acquisition of a 76% interest in Achidatex Nazareth Elite (1977) Ltd. effective June 18, 2001 is not deductible against income generated in Israel for income tax purposes. Depreciation expense with respect to these fixed assets was approximately $36,000 for the three months ended June 30, 2002. There was no similar depreciation expense for the three months ended June 30, 2001.

FINANCIAL INCOME / (EXPENSES), NET

Financial income (expense), net in the three months ended June 30, 2002 were $33,144 compared to $41,012 for the same three months in 2001.

Six Months Ended June 30, 2002 Compared to Six Months Ended June 30, 2001

SALES AND GROSS PROFIT MARGIN

Sales in the six months ended June 30, 2002 increased to $5,313,635 from $2,039,258 for the same six months in 2001. We attribute this increase in sales to the acquisition of Achidatex, Ltd. and increased demand for our products. The breakdown of sales for the six months ended June 30 is as follows:

		2002 ($)	2001 ($)
Sales to the local market-civilian		2,011,659	960,620
Sales to the local market-military		2,506,343	804,102
Export sales-military		795,633	274,536
Totals	$	5,313,635	2,039,258

Sales to the local market increased by 109.4% This increase in sales is explained partly by the acquisition of Achidatex, Ltd. and the increased demand for our products. The gross margin for the six months ended June 30, 2002 improved to 39% as compared to 33% for the same six months in 2001.

Gross profit for the six months ended June 30, 2002 increased to $2,046,527 from $665,269 for the same six months in 2001. This increase in gross profit is explained partly by the acquisition of Achidatex and increased demand for our products.

The cost of production in the six months ended June 30, 2002 was $3,267,108 compared to $1,373,989 for the same six months in 2001. This change in cost of production is explained partly by the acquisition of Achidatex and increased demand for our products.

SELLING, GENERAL AND ADMINISTRATIVE EXPENSES

General and administrative costs in the six months ended June 30, 2002 were $599,165 compared to $264,568 for the same six months in 2001. This change is explained partly by the acquisition of Achidatex, Ltd. and the increased demand for our products.

Unfulfilled open orders at June 30, 2002 totaled $3,000,000 and are scheduled for filling within the next three months.

INCOME TAX EXPENSE

Income tax expense for the six months ended June 30, 2002 was $408,081 or 38.1% of income before income taxes, as compared to $97,743 or 30.8% of income before income taxes for the six months ended June 30, 2001.

The effective income tax rate increased in 2002 as compared to 2001 as a result of several factors. Certain stock-based non-cash operating expenses incurred in 2002 at the US holding company level were not deductible against the income generated at the Israel subsidiaries for income tax purposes. In addition, depreciation expense with respect to fixed assets of approximately $1,441,000 acquired in conjunction with the acquisition of a 76% interest in Achidatex Nazareth Elite (1977) Ltd. effective June 18, 2001 is not deductible against income generated in Israel for income tax purposes. Depreciation expense with respect to these fixed assets was approximately $72,000 for the six months ended June 30, 2002. There was no similar depreciation expense for the six months ended June 30, 2001.

FINANCIAL INCOME / (EXPENSES), NET

Financial income (expense), net in the six months ended June 30, 2002 were $66,295 compared to $30,046 for the same three months in 2001.

LIQUIDITY AND CAPITAL RESOURCES

Our current activities are financed by short and long term bank loans balanced by short term deposits. The decision regarding the amount of the short term loans was derived from considerations of the yield on the deposit which is generally in foreign currency (receipts from overseas sales), compared to the cost of short term loans. We have positive working capital (current assets less current liabilities). Long term loans derived from acquisition of Achidatex, Ltd. their due spread over five years.

During this year and the year following, we anticipate increasing our research and development of certain items, primarily, ballistic helmets, stab-resistant fabric, ceramic ballistic plates, ballistic wall covering and one-way protective windows. We anticipate total research and development expenses for 2002 and 2003 to be approximately $1,950,000 and $750,000 respectively. We anticipate that in the year 2003 research and development expenses will drop to approximately $350,000. The development of these products will be with staff engineers. With respect to ballistic helmets, we anticipate that these products will be approximately in 20% production by the end of this year, increasing to full production by the year 2005. We anticipate that in order to fund the research and development for these products, we may effect an offering of our equity securities. If we are unable to effect an offering of our securities, we may fund our research and development through our operating funds. In such event, the timing of our anticipated research and development and subsequent production schedule would be slowed.

RECENT ACCOUNTING PRONOUNCEMENTS AND CRITICAL ACCOUNTING POLICIES

BASIS OF PRESENTATION

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

PRINCIPLES OF CONSOLIDATION

The condensed consolidated financial statements for 2002 include the accounts of Defense Industries International, Inc. (formerly Pawnbrokers Exchange, Inc. (see Note 7)) 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 (collectively, the "Company"). The minority interest represents the minority shareholders' proportionate share of Achidatex.

The consolidated financial statements for 2001 include the accounts of Export Erez, USA, Inc. and its wholly owned subsidiaries, Export Erez, Ltd., Mayotex, Ltd. and Dragonwear Trading Ltd. and its 76% owned subsidiary Achidatex Nazareth Elite from June 18, 2001, the date of acquisition (See Note 5).

All intercompany accounts and transactions have been eliminated in consolidation.

USE OF ESTIMATES

The preparation of financial statements in conformity with Accounting principles generally accepted in the United States of America 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.

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.

INTERIM CONSOLIDATED FINANCIAL STATEMENTS

The condensed consolidated financial statements as of June 30, 2002 and for the three and six months ended June 30, 2002 and 2001 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 consolidated results of operations for the three and six months ended June 30, 2002 and 2001 are not necessarily indicative of the results to be expected for the full year. The condensed consolidated balance sheet information as of December 31, 2001 was derived from the audited consolidated financial statements included in the Company's annual report Form 10-KSB. The interim condensed consolidated financial statements should be read in conjunction with that report.

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PRIOR PERIOD ADJUSTMENT

The accompanying condensed consolidated balance sheet as of December 31, 2001 has been restated to correct an error for the understatement of depreciation expense during 2001. The effect of the restatement was to decrease net income for 2001 by $72,053. Retained earnings and property, plant and equipment, net in the December 31, 2001 consolidated balance sheet and retained earnings in the consolidated statement of changes in shareholders' equity have been restated for the effects of the prior period adjustment.

PART II. OTHER INFORMATION

Item 1. Legal Proceedings

None.

Item 2. Changes in Securities and Use of Proceeds.

On April 8, 2002 the Company entered into a one year agreement with a consultant whereby the Company issued 100,000 shares of unregistered common stock in return for future consulting services.

On April 30, 2002 the Company entered into a one year agreement with a consultant whereby the Company issued 300,000 shares of unregistered common stock in return for future consulting services. The contract is in dispute. Counsel for the Company is confident that the Company will prevail in receive its 300,000 shares back. (See Note 4 - Shareholders' Equity {B} Issuances of Common Stock).

Item 3. Defaults Upon Senior Securities

None.

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

In June 2002, a majority of the shareholders representing 21,000,000 shares of the 25,000,000 shares outstanding of the common stock as of May 30, 2002, consented in writing to: (1)a change of domicile merger to effect a transfer of the Company's domicile from the State of Utah to the State of Nevada; and (2) adoption of a Stock Option Plan. Reference is made to the information contained in our Definitive Information Statement made pursuant to Section 14(C) of the Securities Exchange Act of 1934, filed with the Securities & Exchange Commission on June 14, 2002.

Item 5. Other Information

None.

Item 6. Exhibits and Reports on Form 8-K

(a) Exhibits:

99.1 Sarbanes-Oxley Certification

(b) Reports on Form 8-K:

None.

SIGNATURES

In accordance with the requirements of the Exchange Act, the Registrant has caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

Dated: August 14, 2002

DEFENSE INDUSTRIES INTERNATIONAL, INC.

By: /s/ Joseph Fostbinder

Name: Joseph Fostbinder
Title: President