DEFENSE INDUSTRIES INTERNATIONAL INC
Form 10QSB
May 23, 2005

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, 2005

[_] 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	84-1421483
(State of Incorporation)	(I.R.S. Employer Identification No.)

8 BRUSSELS ST. SDEROT, 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 23, 2005 the Issuer had 25,386,463 shares of Common Stock, $.0001 par value per share, outstanding.

Transitional Small Business Disclosure Format (check one):

Yes [_] No [X]

DEFENSE INDUSTRIES INTERNATIONAL, INC. AND SUBSIDIARIES

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DEFENSE INDUSTRIES INTERNATIONAL, INC.
AND SUBSIDIARIES
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PART I - FINANCIAL INFORMATION

ITEM 1.

ASSETS

	March 31, 2005 (Unaudited)	Decemb 20
CURRENT ASSETS		
Cash and cash equivalents	$ 528,578	$ 50
Accounts receivable, net of allowance for doubtful accounts		

of $117,821and $105,927, respectively	3,907,328	2,49
Accounts receivable - related parties, net	443,834	37
Inventories	3,178,061	2,80
Investments in marketable securities	851,032	80
Deferred taxes	38,762	4
Other current assets	658,315	40
Total Current Assets	9,605,910	7,43
PROPERTY, PLANT AND EQUIPMENT, NET	2,000,252	1,76
OTHER ASSETS		
Deposits for the severance of employer-employee relations	485,863	48
Deferred taxes, long-term	70,718	6
Intangible assets, net	28,376	3
Goodwill	80,900	
Total Other Assets	665,857	57
TOTAL ASSETS	$12,272,019	$ 9,77

The accompanying notes are an integral part of the condensed consolidated financial statements.

DEFENSE INDUSTRIES INTERNATIONAL, INC.
AND SUBSIDIARIES
CONDENSED CONSOLIDATED BALANCE SHEETS

LIABILITIES AND SHAREHOLDERS' EQUITY

	Ma (
CURRENT LIABILITIES	
Accounts payable	$
Accrued expenses	
Short-term debt	
Current portion of long-term debt	
Common stock to be issued	
Other current liabilities	
Total Current Liabilities	
LONG-TERM LIABILITIES	
Long-term portion of debt	
Provision for the severance of employer-employee relations	
Common stock to be issued	
Minority interest	

Total long-term Liabilities	--
TOTAL LIABILITIES	--
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 shares authorized, 25,350,000 issued and outstanding	
Additional paid-in capital	
Retained earnings	
Accumulated other comprehensive loss	
Total Shareholders' Equity	--
TOTAL LIABILITIES AND SHAREHOLDERS' EQUITY	$

The accompanying notes are an integral part of the condensed consolidated financial statements.

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DEFENSE INDUSTRIES INTERNATIONAL, INC.
AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENTS OF INCOME AND
COMPREHENSIVE INCOME FOR THE THREE MONTHS ENDED MARCH 31, 2005
AND 2004
(UNAUDITED)

	For the Three Months Ended March 31, 2005
NET REVENUES	$ 3,684,480
COST OF SALES	3,029,383
GROSS PROFIT	655,097
OPERATING EXPENSES	
Selling	144,081
General and administrative	397,096

TOTAL OPERATING EXPENSES	541,177
INCOME FROM OPERATIONS	113,920
OTHER INCOME (EXPENSE)	
Financial expense, net	(44,169)
Other income, net	80,226
Total Other Income, net	36,057
INCOME BEFORE INCOME TAXES	149,977
Less: income tax expense	49,014
INCOME BEFORE MINORITY INTEREST	100,963
Minority interest (income) loss	(17,725)
NET INCOME	83,238
OTHER COMPREHENSIVE INCOME	
Foreign currency translation loss, net of minority interest portion	(41,284)
Other comprehensive income before tax	(41,284)
Income tax benefit related to items of other comprehensive income	16,679
TOTAL OTHER COMPREHENSIVE (LOSS), NET OF TAX	(24,605)
COMPREHENSIVE INCOME	$ 58,633
Net income per share - basic and diluted	$ 0.00
Weighted average number of shares outstanding - basic and diluted	25,350,000

The accompanying notes are an integral part of the condensed consolidated financial statements.

DEFENSE INDUSTRIES INTERNATIONAL, INC.
AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS
FOR THE THREE MONTHS ENDED MARCH 31, 2005 AND 2004
(UNAUDITED)

CASH FLOWS FROM OPERATING ACTIVITIES:
Net income
Adjustments to reconcile net income to net cash (used in) provided by operating activities:
Depreciation and amortization
Gain from sale of property, plant and equipment
Provision for doubtful accounts
Net realized and unrealized (gain) loss on marketable securities
Minority interest in income (loss) of subsidiary
Changes in operating assets and liabilities, net of effects of acquisition:
(Increase) decrease in deposits for employee severance
(Increase) decrease in deferred taxes
Increase in accounts receivable
Increase in other current assets
(Increase) decrease in inventories
Increase in accounts payable
Increase in accrued expenses
Decrease in other current liabilities
Increase (decrease) in provision for the severance of employer-employee relations

Net Cash (Used in) Provided By Operating Activities

CASH FLOWS FROM INVESTING ACTIVITIES:
Purchases of property, plant and equipment
Proceeds from sale of property, plant and equipment
Proceeds from sale of marketable securities
Cash acquired in acquisition of Owen Mills Company
Purchases of marketable securities

Net Cash Used in Investing Activities

CASH FLOWS FROM FINANCING ACTIVITIES:
Short-term debt, net
Payments on long-term debt

Net Cash Provided By (Used In) Financing Activities

EFFECT OF CHANGES IN EXCHANGE RATES ON CASH

NET INCREASE IN CASH AND CASH EQUIVALENTS
CASH AND CASH EQUIVALENTS - BEGINNING OF PERIOD

CASH AND CASH EQUIVALENTS - END OF PERIOD

INTEREST PAID

TAXES PAID

SUPPLEMENTAL DISCLOSURE OF NON-CASH INVESTING AND FINANCING ACTIVITIES:

On February 28, 2005, the Company acquired all the outstanding shares of Owen Mills Company for an aggregate of $372,401, consisting of a note payable of $172,401 and $200,000 in common stock of the Company, both of which are to be paid over five years. (See Note 2 for assets and liabilities acquired).

The accompanying notes are an integral part of the condensed consolidated financial statements.

DEFENSE INDUSTRIES INTERNATIONAL, INC.
AND SUBSIDIARIES
NOTES TO CONDENDED CONSOLIDATED FINANCIAL STATEMENTS
FOR THE THREE MONTHS ENDED MARCH 31, 2005 AND 2004
(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 include the accounts of Defense Industries International, Inc. and its wholly owned subsidiaries, Export Erez, USA, Inc., Export Erez, Ltd., Mayotex, Ltd. Dragonwear Trading Ltd. and its 76% owned subsidiary Achidatex Nazareth Elite for all periods presented and Rizzo, Inc. (doing business as Owen Mills Company) since February 28, 2005 (the acquisition date) (collectively, the "Company"). The minority interest represents the minority shareholders' proportionate share of Achidatex and Owen Mills Company.

All intercompany accounts and transactions have been eliminated in consolidation.

(C) USE OF ESTIMATES

The preparation of condensed consolidated 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 condensed consolidated 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 number of common shares outstanding during the period. Diluted net income per common share is computed based on the weighted average number of common shares and common stock equivalents outstanding during the period. There were no common stock equivalents outstanding during the periods presented. Accordingly, a reconciliation between basic and diluted earnings per share is not presented.

DEFENSE INDUSTRIES INTERNATIONAL, INC.

AND SUBSIDIARIES
NOTES TO CONDENDED CONSOLIDATED FINANCIAL STATEMENTS
FOR THE THREE MONTHS ENDED MARCH 31, 2005 AND 2004
(UNAUDITED)

(E) INTERIM CONSOLIDATED FINANCIAL STATEMENTS

The condensed consolidated financial statements as of and for the three months ended March 31, 2005 and 2004 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 months ended March 31, 2005 and 2004 are not necessarily indicative of the results to be expected for the full year. The consolidated balance sheet information as of December 31, 2004 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) GOODWILL AND OTHER INTANGIBLE ASSETS

In accordance with Statement of Financial Accounting Standards ("SFAS") No. 141, the Company allocates the purchase price of its acquisitions to the tangible assets, liabilities and intangible assets acquired based on their estimated fair values. The excess purchase price over those fair values is recorded as goodwill. The fair value assigned to intangible assets acquired is either based on valuations prepared by independent third party appraisal firms using estimates and assumptions provided by management or negotiated at arms-length between the Company and the seller of the acquired assets. In accordance with SFAS No. 142, goodwill and purchased intangibles with indefinite lives are not amortized, but will be reviewed periodically for impairment. Purchased intangibles with finite lives will be amortized on a straight-line basis over their respective useful lives.

NOTE 2 BUSINESS COMBINATION

Effective February 28, 2005, the Company acquired all of the outstanding shares of Rizzo Inc. (doing business as Owen Mills Company), a Los Angeles-based manufacturing and service company specializing in military and industrial sewing of marine and ballistic fabric products. Under the terms of the agreement, the Company purchased all of the outstanding stock of Owen Mills Company in consideration for a $200,000 note payable and shares of the Company's common stock having a value of $200,000, based on the average closing price per share of the Company's common stock for the ten trading days preceding the issuance of such shares. The Company shall pay the $400,000 of consideration as follows: (i) $3,333.33 each month commencing on March 31, 2005 and thereafter on the last business day of each successive month until the Company has paid the former shareholder of Owen Mills Company a total of $200,000; the present value of the payments is $172,401 (ii) $40,000 in the form of shares of common stock of the Company payable within fifteen (15) business days from the date of the Agreement; and (iii) $40,000 in the form of the Company's common stock paid to the former shareholder of Owen Mills Company on each of the last business days of February 2006, February 2007, February 2008, and of February 2009. The Company acquired assets totaling $576,190 (consisting of cash of $20,415, accounts receivable, net of $232,224, inventory of $179,306, property, plant and equipment, net of $140,380, and other current assets of $3,865) and assumed liabilities of $284,689 (consisting of accounts payable of $30,973, other current liabilities of $160,046, and long-term debt of $93,670), which resulted in the recording of $80,900 in goodwill.

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DEFENSE INDUSTRIES INTERNATIONAL, INC.
AND SUBSIDIARIES
NOTES TO CONDENDED CONSOLIDATED FINANCIAL STATEMENTS
FOR THE THREE MONTHS ENDED MARCH 31, 2005 AND 2004
(UNAUDITED)

The acquisition of Owen Mills Company was accounted for as a purchase under SFAS No. 141, Business Combinations. Accordingly, the operating results of Owen Mills Company have been included in the consolidated statements of income after the acquisition date of February 28, 2005. The following table reflects the unaudited pro forma combined results of operations for the three months ended March 31, 2005 and 2004, assuming the acquisition had occurred at the beginning of 2004.

	For the Three Months Ended March 31, 2005	For the Three Months Ended March 31, 2004
Revenue	$3,844,061	$4,017,093
Net income	$ 80,681	$ 353,652
Net income per share - basic and diluted	$ 0.00	$ 0.01

NOTE 3 INVENTORIES

Inventories consisted of the following:

	March 31, 2005	December 31, 2004
Raw materials	$1,772,702	$1,639,456
Work in process	1,149,010	837,836
Finished goods	256,349	331,727
	$3,178,061	$2,809,019

NOTE 4 SEGMENT INFORMATION AND CONCENTRATIONS

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.

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DEFENSE INDUSTRIES INTERNATIONAL, INC.
AND SUBSIDIARIES
NOTES TO CONDENDED CONSOLIDATED FINANCIAL STATEMENTS
FOR THE THREE MONTHS ENDED MARCH 31, 2005 AND 2004
(UNAUDITED)

(A) SALES AND INCOME FROM OPERATIONS:

	Civilian Local	Military Local	Military Export	Consolidated
March 31, 2005				
Net Sales	$ 459,020	$ 581,467	$2,643,993	$3,684,480
Income from operations	10,297	34,786	68,837	113,920
March 31, 2004				
Net Sales	$ 257,087	$ 442,017	$3,046,975	$3,746,079
Income from operations	40,669	99,178	398,776	538,623

(B) SINGLE CUSTOMERS EXCEEDING 10% OF SALES:

	For the Three Months Ended March 31, 2005	For the Three Months Ended March 31, 2004
Sales		
Customer A (Military Export)	-	$1,731,656
Customer B (Military Export)	$ 795,168	-
Customer C (Military Export)	$ 540,428	-
Customer D (Military Export)	$ 515,392	-

NOTE 5 COMMITMENTS AND CONTINGENCIES

During 2004, the Israeli Government decided to evacuate the Erez Industrial Zone in the Gaza Strip where part of operations were located. The Company owns facilities, leases other facilities and maintains equipment and inventory within this area. In 2005, the Company moved its "light cut and sew" operation from the Industrial Zone Erez to Sderot as well as some of its webbing equipment to Nazareth. The Israeli Government's initial decision to evacuate the Gaza Strip was backed by resolutions to compensate the Israeli Gaza Strip settlers as well as business and property owners in the Gaza Strip and in the Erez Industrial Zone. While the Israeli Government has not yet decided on the date of the evacuation, there is no doubt that it will evacuate the area, or that it will come to an agreement with the business and property owners for their compensation. The compensation is mentioned in the "Evacuation Law" resolution that was adopted by the Israeli Parliament, however, the amount of the compensation will be negotiable.

The Company believes that, at a minimum, it will be compensated for the actual expenses incurred in connection with the potential relocation.

NOTE 6 SUBSEQUENT EVENTS

On April 27, 2005, the Company issued 36,463 common shares having a fair value of $40,000 to the former shareholder of Owen Mills Company according to the business combination agreement signed on February 28, 2005. Also see Note 2.

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

THIS INFORMATION SHOULD BE READ IN CONJUNCTION WITH THE CONDENSED CONSOLIDATED FINANCIAL STATEMENTS AND NOTES INCLUDED IN ITEM 1 OF PART I OF THIS QUARTERLY REPORT AND THE AUDITED CONSOLIDATED FINANCIAL STATEMENTS AND NOTES THERETO AND MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS FOR THE YEAR ENDED DECEMBER 31, 2004 CONTAINED IN OUR 2004 ANNUAL REPORT ON FORM 10-KSB. 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 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 condensed consolidated financial statements. The preparation of our consolidated 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 condensed consolidated financial statements and the reported amounts of sales and expenses during the reporting periods. Our condensed 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 upon shipment to customers. 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 March 31, 2005 and March 31, 2004. If we change any of our assumptions with regard to our recognition of revenues, or if there is a change with respect to warranties expenses our financial position and results of operations may change materially.

FOREIGN CURRENCY TRANSLATION AND TRANSACTIONS. The functional currency of Export Erez, Ltd., Mayotex Ltd., and Achidatex Nazareth Elite is the New Israeli Shekel, or NIS. The functional currency of Dragonwear Trading Ltd. is the Cyprus Pound, or 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 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. Any change in exchange rates may have a material impact on our financial position and results of operations.

INVENTORIES. Inventories are valued at the lower of cost or market value using the first-in first-out method. 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. Inventories write-offs and write-down provisions are provided to cover risks arising from slow-moving items or technological obsolescence. Any change in our assumptions with respect to the need to write-off write-down the value of our inventories may have material affect on our financial position or results of operations.

PROPERTY AND EQUIPMENT. Fixed assets are stated at cost less accumulated depreciation. Depreciation is computed using the straight-line method over the 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. The use of different assumptions with respect to the expected cash flows from our assets and other economic variables, primarily the discount rate, may lead to different conclusions regarding the recoverability of our assets' carrying values and to the potential need to recordan impairment loss for our long lived assets.

OVERVIEW

We are 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, bullet proof vests and jackets, ballistic wall coverings, bullet proof ceramic and polyethylene panels, V.I.P. car armoring and lightweight armor kits for vehicles, personal military equipment, dry storage systems, liquid logistic products, tents and other camping and travel gear.

From time to time we have provided bulletproof vests developed by us to laboratories in the United States for testing, and following the tests, the products were deemed to have met the American National Institute of Justice (NIJ) standards. The American NIJ standards are the accepted standards worldwide for bulletproof vests and compliance with these standards has enabled us to enter into the North American market as well as other new markets for our bulletproof vests. Similarly, we have submitted our ballistic ceramic plates for testing by German laboratories and following the tests, the products were deemed to have met the German qualification standard. Obtaining this standard has enabled us to enter the German and other European markets for these products.

Our strategy is to capitalize on our significant research and development capabilities and the strength of our brand identity and achieve greater economies of scale. Due to ever-present international tensions we believe that the demand for our products will continue to grow. We expect to address this growth by offering a comprehensive array of high quality branded security products to meet the needs of our customers around the world. We intend to enhance our leadership position in the industry through additional strategic acquisitions and by creating a broad portfolio of products and services to satisfy all of our customers' increasingly complex security products needs. The following elements define our growth strategy.

- CAPITALIZE ON EXPOSURE TO MILITARY PROBLEMS. We believe that the events of September 11, 2001, the subsequent "War on Terrorism," the continuing conflict in Iraq, the increasing likelihood of military conflicts abroad, and recent events where lives have been saved due to the performance of armor systems, are all likely to result in additional interest in our products.

- EXPAND DISTRIBUTION, NETWORKS AND PRODUCT OFFERINGS. We expect to continue to leverage our distribution network by expanding our range of branded law enforcement equipment through the acquisition of niche defensive security products manufacturers and by investing in the development of new and enhanced products which complement our existing offerings. We believe that a broader product line will strengthen our relationships with distributors and enhance our brand appeal with military, law enforcement and other end users.

- PURSUE STRATEGIC ACQUISITIONS. In addition to our recent acquisition of Owen Mills, we intend to continue selectively pursue strategic acquisitions that complement and/or expand our product offerings, provide access to new geographic markets, and provide additional distribution channels and new customer relations.

OPERATIONS IN EREZ INDUSTRIAL ZONE

During 2004, the Israeli Government decided to evacuate the Erez Industrial Zone in the Gaza Strip where part of our operations are located. We own facilities, lease other facilities and maintain equipment and inventory within this area. The Israeli Government's initial decision to evacuate the Gaza Strip was backed by resolutions to compensate the Israeli Gaza Strip settlers as well as business and property owners in the Gaza Strip and in the Erez Industrial Zone. While the Israeli Government has not yet decided on the date of the evacuation, there is no doubt that it will evacuate the area, or that it will come to an agreement with the business and property owners for their compensation. The compensation is mentioned in the "Evacuation Law" resolution that was adopted by the Israeli Parliament, however, the amount of the compensation will be negotiable.

During the last half of 2004, we prepared for the eventual evacuation by merging existing production facilities. We moved a "light cut and sew" operation from the Erez Industrial Zone to Sderot as well as some of our webbing equipment to Nazareth. The Erez Industrial Zone activity will continue operating and inventories will continue to be maintained there until the evacuation occurs.

Due to the Company's anticipation that it will be reimbursed for all costs related to the evacuation of the Erez Industrial Zone and the fact that the facility is still operating and the equipment will be relocated, no impairment or accrued liabilities have been recorded at March 31, 2005.

THREE MONTHS ENDED MARCH 31, 2005 COMPARED WITH THREE MONTHS ENDED MARCH 31, 2004

RESULTS OF OPERATIONS

NET REVENUES AND GROSS PROFIT MARGIN. Net revenues for the three months ended March 31, 2005 decreased to $3,684,480 from $3,746,079 in the same period in 2004, a decrease of 1.6%. The decrease is attributable to a decrease in export sales. We attribute this decrease in export sales to the fact that a major export customer in 2004 did not contribute to the export sales during the three months ended March 31, 2005. This decrease was partially offset by the continued successful implementation of our growth plan with our focus on the international markets and increased sales to the local markets.

The following table sets forth the breakdown of sales by segment for the three months ended March 31, 2005 and 2004.

	Three Months Ended March 31,	
	2005	2004
Sales to the local civilian market	$ 459,020	$ 257,087
Sales to the local military market	581,467	442,017
Export military sales	2,643,993	3,046,975
Total	$3,684,480	$3,746,079

The dominance of export sales is expected to continue into the second quarter of 2005. This expectation is based, among other things, on the fact that we have broadened our export customers base.

We anticipate that our revenues for the remainder of 2005 will exceed our sales results in the same period in 2004.

Gross profit for the three months ended March 31, 2005 was $655,097 compared to $966,239 for the same period in 2004. This decrease in gross profit is principally attributable to the change in the mix of products sold, which products were characterized by low profit margins, and the temporary lower operating efficiency resulting from the partial relocation of certain manufacturing lines from Erez Industrial Zone to Sderot. As a result, our gross profit margin for the three months ended March 31, 2005 was 17.8% compared to 25.8% for the same period in 2004. We anticipate an increase in our gross profit margin in the second quarter of 2005. Also affecting our gross profits in the three months ended March 31, 2005 was the approximate 5.9% increase in the ratio between the Euro (which is the currency used for the majority of our raw material purchases) and the US Dollar (which is the principal currency for our sales). We believe that the second quarter of 2005 will be characterized by an increased demand worldwide for raw materials, that may result in significant extensions in the regular delivery schedules and an increase in raw material prices which will likely effect our cost of production.

SELLING EXPENSES. Selling expenses for the three months ended March 31, 2005 increased to $144,081 from $120,919 for the same the same period in 2004. The increase in our selling expenses was attributable to higher commission payments on sales to a major export customer.

GENERAL AND ADMINISTRATIVE EXPENSES. General and administrative expenses for three months ended March 31, 2005 increased to $397,096 from $306,697 for the same period in 2004. This increase is mainly a result of our activity to expand our presence in the United States and costs associated with the partial relocation of certain manufacturing lines from Erez Industrial Zone to Sderot. We do not anticipate any material change in our general and administrative expenses in the second quarter of 2005.

INCOME TAX EXPENSE. Our income tax expense for the three months ended March 31, 2005 was $49,014 as compared to a tax expense of $194,338 for the comparable period in 2004, reflecting the lower level of earnings in the first quarter of 2005. Our effective tax rate was 32.7 % in the 2005 period, compared to 35.9% in the 2004 period.

FINANCIAL EXPENSES. We had financial expenses, net of $44,169 for the three months ended March 31, 2005 as compared to $24,482 for the same period in 2004. This increase is attributed mainly to the increase in the rate of exchange between the U.S. Dollar ($) and the New Israeli Shekel (NIS).

OTHER INCOME, NET. We had other income, net for the three months ended March 31, 2005 of $80,226 as compared to other income of $27,198 for the same period in 2004. The increase in other income, net is attributable to income from our marketable securities.

LIQUIDITY AND CAPITAL RESOURCES

As of March 31, 2005, we had $528,578 in cash and cash equivalents, $851,032 in marketable securities and working capital of $4,275,626 as compared to $505,013 in cash and cash equivalents, $808,102 in marketable securities and $4,344,566 in working capital on December 31, 2004. The decrease in working capital is mainly due to our acquisition of Owen Mills Company in March 2005 and purchase of fixed assets.

Net cash used by operating activities was $452,172 for the three months ended March 31, 2005. This was primarily attributable to a $1,253,398 increase in accounts receivable due to an increase in export sales from the forth quarter of 2004, a $252,125 increase in other current assets, a $190,435 increase in other current liabilities and a $ 189,736 increase in inventories, which was offset by, among other things, $83,238 of net income, and a $97,553 increase in accounts payable.

Net cash used for investing activities was $141,418 for the three months ended March 31, 2005. During the three months ended March 31, 2005, $186,128 was used to purchase property, plant and equipment, while $17,794 was provided from sales of fixed assets, and $20,415 was obtained in connection with the acquisition of Owen Mills in February 2005.

Net cash provided from financing activities was $628,928 for the three months ended March 31, 2005. During the three months ended March 31, 2005, we increased our short-term debt by $787,353, net and we repaid long term debt of $158,425.

We believe that we have sufficient working capital and borrowing capability to sustain our current level of operations for the next twelve months.

We anticipate that our research and development expenses for the remainder of 2005 and for 2006 will reflect annualized spending of approximately $250,000 per year. If we are unable to affect a financing that will provide for research and development and other corporate purposes, we will fund our research and development through our operating funds. In such event, the pace of our anticipated research and development and subsequent production schedule would be delayed.

FOREIGN CURRENCY EXCHANGE RISK

We develop products in Israel and sell them in South America, Asia and several European countries. As a result, our financial results could be affected by factors such as changes in foreign currency exchange rates or weak economic conditions in foreign markets.

Our foreign currency exposure with respect to our sales is mitigated, and we expect it will continue to be mitigated, through salaries, materials and support operations, in which part of these costs are denominated in NIS.

During 2004, the NIS appreciated in value in relation to the dollar by approximately 2.35% against the U.S. dollar. In the first quarter of 2005 the NIS appreciated in value in relation to the dollar by approximately 1.28 % against the U.S. dollar. Among the factors contributing to the appreciation in NIS value in relation to the dollar is the low interest rate for US investments compared to the higher interest rate for Israeli investments. The deflation in Israel was approximately 0.6% for the three months ended March 31, 2005 compared to an annual deflation of 1.2% in 2004.

Since most of our sales are quoted in U.S. dollars, and a portion of our expenses are incurred in NIS, our results may be adversely affected by a change in the rate of inflation in Israel or if such change in the rate of inflation is not offset, or is offset on a lagging basis, by a corresponding devaluation of the NIS against the U.S. dollar and other foreign currencies. We will also be adversely affected if the U.S. dollar continues to depreciate against the Euro, the currency used for many of our purchases of raw material.

We did not enter into any foreign exchange contracts in 2004 or the first three months of 2005.

CONTRACTUAL OBLIGATIONS

The following table summarizes our contractual obligations and commercial commitments as of March 31, 2005.

Contractual Obligations	Payments due by Period				
	Total	less than 1 year	2-3 years	4-5 years	more yea
Long-term debt obligations	1,232,500	422,287	602,972	207,241	
Capital (finance) lease obligations	-	-	-	-	
Operating lease obligations	736,100	255,600	468,000	12,500	
Purchase obligations	-	-	-	-	
Other long-term liabilities					

reflected on the Company's balance sheet under U.S. GAAP	-	-	-	-	-
Total	1,968,600	677,887	1,070,972	219,741	

CAUTIONARY STATEMENT REGARDING FORWARD-LOOKING INFORMATION AND RISK FACTORS

THIS REPORT CONTAINS FORWARD-LOOKING STATEMENTS WITHIN THE MEANING OF THE PRIVATE SECURITIES LITIGATION REFORM ACT OF 1995. WORDS SUCH AS "ANTICIPATE," "EXPECT," "INTEND," "PLAN," "BELIEVE," "SEEK," "OUTLOOK" AND "ESTIMATE" AS WELL AS SIMILAR WORDS AND PHRASES SIGNIFY FORWARD-LOOKING STATEMENTS. OUR FORWARD-LOOKING STATEMENTS ARE NOT GUARANTEES OF FUTURE RESULTS AND CONDITIONS AND IMPORTANT FACTORS, RISKS AND UNCERTAINTIES MAY CAUSE OUR ACTUAL RESULTS TO DIFFER MATERIALLY FROM THOSE EXPRESSED IN OUR FORWARD-LOOKING STATEMENTS. THESE UNCERTAINTIES AND OTHER FACTORS INCLUDE, BUT ARE NOT LIMITED TO, THE FOLLOWING:

- Our products are used in applications that are inherently risky and could give rise to product liability and other claims arising from the design, manufacture or sale of such goods. If we are found to be liable in such claim we may be required to pay substantial damages and our insurance costs may increase significantly. Moreover, our insurance coverage may not be sufficient to cover the payment of any potential claim. As a result of such claim, insurance coverage will may not be available for us. The inability to obtain product liability coverage would prohibit us from bidding for orders from certain governmental customers.

- Our failure or inability to comply with extensive government regulation to which we are subject could materially restrict our operations and subject us to substantial penalties.

- Our significant international operations subject us to financial and regulatory risks.

- Currency exchange rate fluctuations in the world markets in which we conduct business could have a material adverse effect on our business, results of operations and financial condition.

- Reduction in military budgets worldwide may cause a reduction in our revenues.

- Sales of our products are subject to governmental procurement procedures and practices; termination, reduction or modification of contracts with our customers, and especially with the government of Israel, or a substantial decrease in our customers' budgets may adversely affect on us.

- The loss of one or more of our key customers would result in a loss of a significant amount of our revenues.

- Our markets are highly competitive. Inability to compete effectively will adversely affect us.

- Limited sources for some of our raw materials may significantly curtail our manufacturing operations.

- Our resources may be insufficient to manage the demands imposed by any future growth.

- Technological advances, the introduction of new products, and new design and manufacturing techniques could adversely affect our operations unless we are able to adapt to the resulting change in conditions.

- We may need to raise additional capital in the future, which may not be available to us.

- Conditions in Israel affect our operations and may limit our ability to produce and sell our products, which could decrease our revenues.

- The economic conditions in Israel have not been stable in recent years.

- Some of our directors, officers and employees are obligated to perform annual military reserve duty in Israel. We cannot assess the potential impact of these obligations on our business.

- Our common stock is thinly traded.

- We are subject to the penny stock rules. These rules may adversely effect trading in our common shares.

- We do not intend to pay dividends.

ITEM 3. CONTROLS AND PROCEDURES

Our management, including our chief executive officer and chief financial officer, evaluated the effectiveness of our disclosure controls and procedures (as defined in Exchange Act Rule 13a-15(e)) as of the end of the period covered by this quarterly report on Form 10-QSB. Based upon that evaluation, our chief executive officer and chief financial officer have concluded that, as of such date, our disclosure controls and procedures were effective to ensure that information required to be disclosed by our company in reports that we file or submit under the U.S. Securities Exchange Act of 1934, as amended, is recorded, processed, summarized and reported within the time periods specified in the Securities and Exchange Commission's rules and forms and that such information was made known to them by others within the company, as appropriate to allow timely decisions regarding required disclosure.

There were no changes to our internal control over financial reporting that occurred during the period covered by this quarterly report on Form 10-QSB that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting

All internal control systems, no matter how well designed, have inherent limitations. Therefore, even those systems determined to be effective may not prevent or detect misstatements and can provide only reasonable assurance with respect to financial statement preparation and presentation. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

PART II - OTHER INFORMATION

DEFENSE INDUSTRIES INTERNATIONAL, INC. AND SUBSIDIARIES

ITEM 1. LEGAL PROCEEDINGS

We are not a party to any pending or to the best of our knowledge, any threatening legal proceedings. None of our directors, officers or affiliates, or owner of record of more than five percent (5%) of our shares, or any affiliate of any such director, officer or security holder is a party adverse to us or has a material interest adverse to us in reference to a pending litigation.

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ITEM 2. UNREGISTERED SALES OF EQUITY SECURITIES AND USE OF PROCEEDS

On February 28, 2005 we entered into an agreement of purchase and sale of stock with Owen Mills Company, a Los Angeles based manufacturing and service company specializing in military and industrial sewing of marine and ballistic fabric products. Under the terms of the agreement, we purchased all of Owen Mills Company's outstanding stock in consideration for $200,000 in cash and shares of our common stock having a value of $200,000, based on the average closing price per share of our shares of common stock for the ten trading days preceding the issuance of such shares. The issuance of shares was made pursuant to an exemption from registration under section 4(2) of the Securities Act of 1933.

ITEM 3. DEFAULT UPON SENIOR SECURITIES

None.

ITEM 4. SUBMISSION OF MATTERS TO A VOTE OF SHAREHOLDERS

None.

ITEM 6. EXHIBITS

(A) EXHIBITS

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

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

32.1 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.

32.2 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.

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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)

/S/ Joseph Postbinder

Joseph Postbinder
Chief Executive Officer

/S/ Tsippy Moldovan

Tsippy Moldovan
Chief Accounting and Financial Officer

Date: May 23, 2005