

China Direct, Inc.
Form 10-Q
August 07, 2008

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

(Mark One)

Form 10-Q

QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
For the quarterly period ended June 30, 2008

or

TRANSITION REPORT UNDER SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
For the transition period from _____ to _____

Commission file number: 001-33694

CHINA DIRECT, INC.

(Exact name of registrant as specified in its charter)

Florida

(State or other jurisdiction of incorporation or organization)

13-3876100

(I.R.S. Employer Identification No.)

431 Fairway Drive, Suite 200, Deerfield Beach, Florida
(Address of principal executive offices)

33441
(Zip Code)

954-363-7333

(Registrant's telephone number, including area code)

Not Applicable

(Former name, former address and former fiscal year, if changed since last report)

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 such filing requirements for the past 90 days.

Yes No

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company. See the definitions of "large accelerated filer," "accelerated filer" and "smaller reporting company" in Rule 12b-2 of the Exchange Act.

Large accelerated filer Accelerated filer

Non-accelerated filer Smaller reporting company
(Do not check if smaller reporting company)

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act)

Yes No

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Indicate the number of shares outstanding of each of the issuer's classes of common stock, as of the latest practicable date. 23,503,916 shares of common stock are issued and outstanding as of August 7, 2008.

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ORGANIZATIONAL CHART

We operate our company in two primary divisions. Our Management Services division acquires controlling interests of Chinese business entities which we consolidate as either our wholly or majority owned subsidiaries. Our Advisory Services division provides consulting services to Chinese entities seeking access to the U.S. capital markets. The following chart reflects our current organizational structure.

INDEX OF CERTAIN DEFINED TERMS USED IN THIS REPORT

When used in this report the terms:

- “China Direct”, “we”, “us” or “our” refers to China Direct, Inc., a Florida corporation, and our subsidiaries,
- “China Direct Investments”, refers to China Direct Investments, Inc., a Florida corporation and a wholly owned subsidiary of China Direct,
- “CDI China”, refers to CDI China, Inc., a Florida corporation, and a wholly owned subsidiary of China Direct,
- “CDI Shanghai Management”, refers to CDI Shanghai Management Co., Ltd., a Chinese limited liability company and a wholly owned subsidiary of CDI China,
- “Capital One Resource”, refers to Capital One Resource Co., Ltd., a Brunei company and a wholly owned subsidiary of CDI Shanghai Management,
- “Lang Chemical”, refers to Shanghai Lang Chemical Co., Ltd. a Chinese limited liability company and a 51% majority owned subsidiary of CDI China,
- “Chang Magnesium”, refers to Taiyuan Changxin Magnesium Co., Ltd., a Chinese limited liability company and a 51% majority owned subsidiary of CDI China,
- “Chang Trading”, refers to Taiyuan Changxin YiWei Trading Co., Ltd., a Chinese limited liability company and a wholly owned subsidiary of Chang Magnesium,
- “Excel Rise”, refers to Excel Rise Technology Co., Ltd., a Brunei company and a wholly owned subsidiary of Chang Magnesium,
- “CDI Magnesium”, refers to CDI Magnesium Co., Ltd., a Brunei company and a 51% majority owned subsidiary of Capital One Resource,
- “Asia Magnesium”, refers to Asia Magnesium Corporation Ltd., a Hong Kong limited liability company and a wholly owned subsidiary of Capital One Resource
- “Golden Magnesium”, refers to Shanxi Gu County Golden Magnesium Co., Ltd., a Chinese limited liability company, formerly referred to by us in filings and press releases as “Jinwei Magnesium”, and a 52% majority owned subsidiary of Asia Magnesium,
- “Pan Asia Magnesium”, refers to Pan Asia Magnesium Co., Ltd., a Chinese limited liability company and a 51% majority owned subsidiary of CDI China,
- “Baotou Changxin Magnesium”, refers to Baotou Changxin Magnesium Co., Ltd., a Chinese limited liability company and a 51% majority owned subsidiary of CDI China,
- “Xinjin Magnesium”, refers to Baotou Xinjin Magnesium Co., Ltd., a Chinese limited liability company. In April 2008 CDI China entered into an agreement to acquire a 51% majority owned subsidiary of Xinjin Magnesium,
- “CDI Clean Technology”, refers to CDI Clean Technology Group, Inc., a Florida corporation formerly known as Jinan Alternative Energy Group Corp., and a wholly owned subsidiary of CDI China,
- “CDI Wanda”, refers to Shandong CDI Wanda New Energy Co., Ltd., a Chinese limited liability company and a 51% majority owned subsidiary of CDI Clean Technology,
- “Yantai CDI Wanda”, refers to Yantai CDI Wanda Renewable Resources Co., Ltd., a Chinese limited liability company and a 52% majority owned subsidiary of CDI Wanda,
- “CDI Jingkun Zinc”, refers to CDI Jingkun Zinc Industry Co., Ltd., a Chinese limited liability company and a 95% majority owned subsidiary of CDI Shanghai Management,
- “CDI Jixiang Metal”, refers to CDI Jixiang Metal Co., Ltd., a Chinese limited liability company and a wholly owned subsidiary of CDI China
- “CDI Metal Recycling”, refers to Shanghai CDI Metal Recycling Co., Ltd., a Chinese limited liability company and an 83% majority owned subsidiary of CDI Shanghai Management
- “CDI Beijing”, refers to CDI (Beijing) International Trading Co., Ltd, a Chinese limited liability company.

PART 1 - FINANCIAL INFORMATION

Item 1. Financial Statements.

CHINA DIRECT, INC. AND SUBSIDIARIES
CONSOLIDATED BALANCE SHEETS

	June 30, 2008	December 31, 2007
	Unaudited	
ASSETS		
Current Assets:		
Cash and cash equivalents	\$ 26,424,935	\$ 20,394,931
Investment in marketable securities available for sale	4,732,593	7,820,500
Investment in marketable securities available for sale-related party	766,019	1,315,488
Accounts receivable, net of allowance for doubtful accounts of \$335,851 and \$290,456 at June 30, 2008 and December 31, 2007, respectively	24,415,061	10,655,661
Accounts receivable-related parties	556,687	2,283,600
Inventories	12,286,538	5,293,986
Prepaid expenses and other current assets	21,564,895	15,439,462
Prepaid expenses-related parties	4,821,163	4,150,943
Loans receivable-related parties	1,597,305	—
Due from related parties	14,552	1,287,877
Total current assets	97,179,748	68,642,448
Restricted cash	2,874	646,970
Property, plant and equipment, net of accumulated depreciation of \$1,499,088 and \$577,801 at June 30, 2008 and December 31, 2007, respectively	25,650,264	18,010,524
Prepaid expenses and other assets	234,683	433,075
Property use rights, net	582,733	553,304
Total assets	\$ 123,650,302	\$ 88,286,321
LIABILITIES AND STOCKHOLDERS' EQUITY		
Current Liabilities:		
Loans payable-short term	\$ 1,229,663	\$ 1,978,142
Accounts payable and accrued expenses	11,584,094	9,649,797
Accounts payable-related parties	735,184	964,114
Notes payable-related party	—	410,167
Accrued dividends payable	20,015	—
Advances from customers	5,785,605	6,963,061
Other payables	6,229,216	4,097,716
Taxes payable	943,779	560,116
Due to related parties	576,890	3,137,233
Total current liabilities	27,104,446	27,760,346
Loans payable-long term	210,280	166,573

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Minority interest	26,351,743	17,535,909
Stockholders' Equity:		
Preferred Stock: \$.0001 par value, stated value \$1,000 per share; 10,000,000 authorized, 1,006 shares and 0 shares issued and outstanding at June 30, 2008 and December 31, 2007, respectively	1,006,250	—
Common Stock: \$.0001 par value, 1,000,000,000 authorized, 23,501,056 and 20,982,010 issued and outstanding at June 30, 2008 and December 31, 2007, respectively	2,350	2,098
Additional paid-in capital	50,654,559	30,257,644
Deferred compensation	(33,000)	(55,000)
Accumulated comprehensive income	36,076	162,045
Retained earnings	18,317,598	12,456,706
Total stockholders' equity	69,983,833	42,823,493
Total liabilities and stockholders' equity	\$ 123,650,302	\$ 88,286,321

See notes to unaudited consolidated financial statements

CHINA DIRECT, INC. AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF OPERATIONS
(Unaudited)

	For the Three Months Ended June 30,		For the Six Months Ended June 30,	
	2008	2007	2008	2007
Revenues	\$ 76,215,437	\$ 40,012,970	\$ 135,456,235	\$ 70,511,910
Revenues-related parties	1,344,725	440,000	2,078,646	880,000
Total revenues	77,560,162	40,452,970	137,534,881	71,391,910
Cost of revenues	64,045,927	36,742,381	113,525,741	64,209,395
Gross profit	13,514,235	3,710,589	24,009,140	7,182,515
Operating expenses:				
Selling, general, and administrative	2,635,633	847,417	4,335,603	1,684,926
Operating income	10,878,602	2,863,172	19,673,537	5,497,589
Other income (expense):				
Other income	102,521	371,433	296,139	381,369
Interest income	129,470	41,855	220,172	71,021
Realized gain (loss) on sale of marketable securities	3,756	206,236	(35,705)	206,236
Realized loss on sale of marketable securities-related party	—	(16,041)	—	(32,014)
Total other income	235,747	603,483	480,606	626,612
Income before income taxes and minority interest	11,114,349	3,466,655	20,154,143	6,124,201
Income tax expense	(705,176)	(522,159)	(1,157,656)	(754,731)
Income before minority interest	10,409,173	2,944,496	18,996,487	5,369,470
Minority interest	(2,894,298)	(676,754)	(6,728,736)	(1,230,859)
Net income	7,514,875	2,267,742	12,267,751	4,138,611

Deduct dividends on Series A Preferred Stock:

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Preferred stock dividend	(1,047,937)	—	(1,189,467)	—
Relative fair value of detachable warrants issued	—	—	(2,765,946)	—
Preferred stock beneficial conversion feature	—	—	(2,451,446)	—

Income applicable to common stockholders	\$ 6,466,938	\$ 2,267,742	\$ 5,860,892	\$ 4,138,611
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Basic and diluted income per common share after deduction in the first quarter of 2008, of noncash deemed dividends attributable to Series A Preferred Stock as described in Notes 3 & 11 of the Notes to the Unaudited Consolidated Financial Statements:

Basic	\$ 0.29	\$ 0.16	\$ 0.27	\$ 0.31
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Diluted	\$ 0.26	\$ 0.15	\$ 0.24	\$ 0.27
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Basic weighted average common shares outstanding	22,663,337	13,882,955	21,833,388	13,464,666
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Diluted weighted average common shares outstanding	25,427,385	15,380,420	24,160,683	15,174,110
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See notes to unaudited consolidated financial statements

CHINA DIRECT, INC. AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF CASH FLOWS
(Unaudited)

	For the Six Months Ended June 30,	
	2008	2007
Cash flows from operating activities:		
Net income	\$ 12,267,751	\$ 4,138,611
Adjustments to reconcile net income to net cash (used in) provided by operating activities:		
Depreciation	921,287	122,810
Bad debt recovery	—	(102,126)
Allowance for doubtful accounts	45,395	—
Stock based compensation	848,364	196,010
Realized gain on investment in marketable securities	35,705	(206,236)
Realized loss on investment in marketable securities-related party	—	32,014
Fair value of securities received for services	(392,942)	(3,275,450)
Minority interest	8,815,834	1,230,859
Changes in operating assets and liabilities:		
Prepaid expenses and other current assets	(4,857,996)	(4,189,986)
Prepaid expenses-related parties	(670,220)	(418,875)
Inventories	(6,992,552)	4,523,227
Accounts receivable		