

Investment



Jay Lichter of Avalon Ventures says his firm has a new way for pharma and venture capital to work together.
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Open Space Draws Retailers on the Move

PROPERTY: Location Options Are Limited in Tight Market

■ By LOU HIRSH

Vacated San Diego County retail space often doesn't stay empty for long, a continuing trend illustrated by cases like the recent closure of a **Kmart** store in Mission Valley.

By year's end, that 120,000-square-foot building will be occupied by the second local store of furniture retailer **Living Spaces**, according to the brokerage firm **CBRE**, which brokered the leasing deal on behalf of the building's owner, **Sears Holdings Corp.**

Mike Moser, a senior vice president in **CBRE's** San Diego office who was involved in the transaction, said the owner had be-



Courtesy of CoStar Group
This Mission Valley building owned by **Sears Holdings Corp.**, which most recently housed a **Kmart** store that is now closed, is being leased to furniture retailer **Living Spaces**, which will open by year's end, according to **CBRE**.

gun fielding queries from several prospective tenants well before the struggling **Kmart** store actually shut its doors. It's a reflection of a market where new retail construction remains

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Air Force Steers Away From Global Hawk

DEFENSE: Northrop Grumman's Drone Is Big Part of Navy's Plans

■ By BRAD GRAVES

The recently released White House budget request for 2014 allocates fewer dollars to **Global Hawk**, **Northrop Grumman's** high-flying unmanned spy plane.

A U.S. Air Force spokesman said the new budget request calls for \$134 million in research and development, as well as \$68 million in procurement for **Global Hawk**.

And while the U.S. Navy plans to eventually field a version of **Global Hawk** — as many as 65 aircraft, one defense analyst said — the near-term forecast for the Air Force version

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Layoff Threat for 665 Is Lifted at Nassco

DEFENSE: Signed Bill Clears Way for Some Planned Work

■ By BRAD GRAVES

A changed federal budget picture means that the **General Dynamics Nassco** shipyard will not have to go through with 665 layoffs announced earlier this year.

Some 375 workers and 290 subcontractors will continue to work, said spokeswoman **Sarah Strang**.

"We felt comfortable we wouldn't need to do any layoffs at this time," Strang said.

Earlier this year, the U.S. Navy warned that it may need to cancel as many as 10 ship visits

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SKIN IN THE GAME

Melissa Jacobs
Simon Craw, left, and Donna Queen of **Lifeline Skin Care Inc.** are in the molecular biology laboratory. **Lifeline** is a wholly owned subsidiary of **International Stem Cell Corp.**

RESEARCH: Biotech Innovations Are Fueling Cosmeceutical Competition

■ By MEGHANA KESHAVAN

A handful of San Diego companies are competing in the lucrative high-end skincare market, using a grounding in real science to produce and promote their beauty wares.

This development is evident in the recent \$350 million acquisition of Carlsbad-based skin care company **SkinMedica Inc.** by Irvine-based drugmaker **Allergan Inc.**

Other local biotechnology outfits are also learning that their science has true value in the growing anti-aging skin cream market.

\$32B

The value the global cosmeceutical market is expected to reach in 2016.

Carlsbad's **International Stem Cell Corp.** is borrowing technology from its medical research to formulate a new line of regenerative skin care products. Encinitas-based **Senté Inc.** was launched by two high-profile San Diego pharmaceutical executives, repurposing a substance used to treat burn victims to develop a cosmetic lotion. And **Skin Authority Inc.** in Carlsbad has partnered with **Dole Food Co. Inc.** to develop Vitamin D-rich skin creams, relying on peer-reviewed literature and medical advisory committees to inform its product development.

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Firm Wants to Change Real Estate Landscape

PROPERTY: Avison Young Brings Its Model to Local Market

■ By LOU HIRSH

Toronto-based commercial real estate services firm **Avison Young** is rapidly growing its own U.S. office footprint, most recently entering a competitive San Diego market already filled with several established regional and national brokerage players.

Chairman and CEO **Mark Rose** said the 35-year-old company, Canada's largest independently owned commercial real estate firm, is looking not only to capitalize on an improving market,



Mark Rose

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Skin:

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All of the San Diego companies tout superior results in small clinical trials, and are using the science in the beauty equation to market their products.

'Incredible Growth'

"Skin care is interesting because it's such a burgeoning field — it's got incredible growth associated with it," said **Faheem Hasnain**, chairman of the board of Senté and chief executive of San Diego pharmaceutical company **Receptos Inc.** "When you start studying the intricacies and possibilities seen in regenerative science, you realize that there's real demand for good high quality products that can actually make a difference."

Called "cosmeceuticals," these products are comprised of biologically active ingredients that are purported to have medical benefits. They tend to occupy a select and high-priced portion of the market, sold primarily in spas, medical practices or online.

The first wave of cosmeceuticals came in the 1990s when alpha-hydroxy complexes hit the shelves, but in recent years, stem cell-based regenerative compounds — as seen in the San Diego companies — have proven popular among company consumers.

The global cosmeceuticals market is growing 7.7 percent each year, and should reach about \$32 billion by 2016, according to a report from market research firm **Global Information Inc.** The report found that while major segments include tooth whitening and lip protection are key market drivers, regenerative skin products are taking hold in a major way.

"New ingredients, such as stem cell and peptides for skincare-based cosmetics, are anticipated to alter the market landscape in the near future," the report said.

Larger companies have taken notice. Allergan, a \$33 billion market cap company whose top selling products include Botox and eyelash growth formula Latisse, took interest in SkinMedica's full line of regenerative skin creams and acquired the private company last December. SkinMedica's sales, at that point, had risen to about \$65 million.

The acquisition was made to direct the company to "take a leadership position in the growing 'physician dispensed'



Photo courtesy of Art of Skin MD
Melanie Palm, a cosmetic dermatologist with a private practice in Solana Beach called the Art of Skin MD, says that the trend toward marketing high-end skin creams is on an upswing.

topical aesthetics skin care category," Allergan president and chief executive **David Pyott** said in a statement.

And a recent bidding war for Long Beach-based anti-aging skin cream maker **Obagi Medical Products Inc.** culminated last week in a \$418 million sale to Montreal-based **Valeant Pharmaceuticals International Inc.**

Donna Queen, a former top Obagi executive, was recruited in 2011 by the International Stem Cell Corp. to lead its wholly owned skin care subsidiary, **Lifeline Skin Care**. The creams are based on certain chemicals excreted by stem cells that have been shown to help stimulate cellular growth and allow skin to look rejuvenated, according to the company.

The revenue from Lifeline helps subsidize the medical research done by the ISCC, whose primary focus is its stem cell-based therapies for Parkinson's disease.

"It's very capital-intensive to run a stem cell and regenerative medicine company, so we came up with the idea for this company as we were looking for creative ways that could generate income without diluting stockholders' shares," said **Simon Crow**, chief operating officer of Lifeline and executive vice president of the ISCC.

The company brought in about \$2.2

million in sales last year from Lifeline, and much of it was routed directly to finance Parkinson's research. The products run from \$97 to \$190 per bottle. Sales are solid and expected to increase dramatically this year, Queen said.

"We're concentrating on professional channels — dermatologists, plastic surgeons and spas who recommend the product to a patient or a client," Queen said. "Retail is more smoke and mirrors, but physicians can see through that. They want more advanced products than are available in department stores — in fact, they demand that."

Melanie Palm, a cosmetic dermatologist with a private practice in Solana Beach called the **Art of Skin MD**, said that the trend toward marketing these high-end creams is on an upswing.

"Some of these biotechnology companies see cosmeceuticals as a great opportunity in the aesthetic market to bolster sales and hit an untapped portion of the market," Palm said.

Palm sells such regenerative products in her office, and sometimes recommends that patients use them to speed up recovery after intensive medical cosmetic procedures. She said that the recent influx of high-profile marketing of regenerative skin creams is motivating patients to request these products from

their doctors.

"Hopefully the physicians are really scrutinizing these products, and actually feel comfortable endorsing them," Palm said. "One thing I do see is the climate's a little tense between academics and private medicine over this issue — and the majority of dermatologists recommending cosmeceuticals are probably in private practice."

This, however, isn't always the case. Senté recently forged a contract with San Diego's Scripps Health to sell its Dermal Repair Cream at various dermatology offices in the health care system's network. The cream is priced at either \$75 or \$165 per bottle, depending on the size.

Senté was formed in 2007 by Hasnain of Receptos and **Kleanthis Xanthopoulos**, president and CEO of San Diego pharmaceutical company **Regulus Therapeutics Inc.**

After several years of development and medical testing, the company began marketing its first skin care cream last fall. It's available in about 50 medical practices around the country. The company plans to quickly begin scaling up its production capabilities, having just announced a \$2.1 million Series B funding round from private investors.

"We built the company and the product to focus on an audience that's the most discerning around the science — most notably, dermatologists, and we want to really ensure that they understand the merits of our product, and the merits of our science," Hasnain said.

Reaching More Customers

Celeste Hilling, president and CEO of **Skin Authority**, is taking a different approach to marketing her regenerative skin care products.

"Some physicians do carry our products, and spas and resorts, but the fact is that three out of four North Americans will have some form of skin cancer in their lives," Hilling said. "We're not reaching that many of them in a single doctor's office or in a beauty store. Our goal is to reach out, and target larger volumes of consumers."

Hilling's products range from \$25 to \$150, and will be sold beginning in May in 150 GNC stores across the country.

"While the different San Diego skin care companies may have different angles on the tech side, we all know the future — and we're embarking on this new generation of skin care products that's going to be about regeneration and prevention," Hilling said.

Retail:

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scarce, with very few large spaces available in existing high-profile centers to meet the needs of retailers and restaurant chains seeking to expand their San Diego presence.

Smaller spaces, in the range of 2,400 to 3,600 square feet, have also become tough to find in centralized markets like Mission Valley.

"It's generally been tightening up," said Moser. "There's less space available than there was a year ago, and you're seeing rents going up as a trend in several places throughout the county."

According to **CoStar Group**, the San Diego region's retail property vacancy rate stood at 4.6 percent at the end of the first quarter, the seventh-lowest among the nation's largest metro markets.

On the metric of retail availability, which includes currently occupied space being marketed by owners because those

leases are expiring, San Diego's figure is 5.9 percent, tied with Miami, Fla., for third-lowest in the nation. Only Honolulu (3.7 percent) and San Francisco (4 percent) have lower availability.

Sam Tenenbaum, a real estate economist with CoStar Group, said much of the San Diego region's 702,710 square feet of positive retail space absorption in the final quarter of 2012 resulted from the completion of a new retail center in San Ysidro — Plaza at the Border, developed by **The Shamrock Group** of Solana Beach — which was nearly fully pre-leased at the time it opened.

In the first quarter of 2013, the local region followed up with an additional 242,740 square feet of positive retail absorption, on par with the prior quarter and up considerably from a year ago. There remain just a few scattered new retail centers in the local construction pipeline, including three in South County, but those likely won't be delivered until 2014 or 2015 at the earliest.

Rising Consumer Confidence

CoStar economist **Ryan McCullough** said the improving national employment climate and rising home sales are helping to boost consumer confidence, which is also supporting retail spending. However, the trend varies by region and income group, and even among submarkets within metro regions.

Most U.S. regions have not reached the point where the housing market is sparking major new shopping center construction, partly because there remains a lot of unused inventory. "There's usually a lag time of 6 to 8 quarters before you see a noticeable increase in retail demand after home sales begin to rise," McCullough said.

Officials of La Mirada-based **Living Spaces** were not immediately available for comment, but the Mission Valley store will be its second in San Diego County. In 2011, it opened in a Vista space previously occupied by **Sam's Club**.

The improving housing market has

fueled local expansion by other furniture and home improvement retailers, such as **Lowe's** and locally based **Fixtures Living**. Other locally based firms, such as **Jerome's Furniture** and **Mor Furniture for Less**, have been expanding outside of San Diego County.

According to local brokerage firms' reports, big retail property sales transactions of the first quarter included **Kimco Realty Corp.**'s \$98 million deal to acquire its institutional partner's half-ownership stake in Santee Trolley Square; **Retail Opportunity Investment Corp.**'s \$12.4 million acquisition of Bernardo Heights Plaza in Rancho Bernardo; and the \$8.1 million purchase of Tierra Corners Shopping Center in Chula Vista, by **JBM Tierra Corners LLC**.

Large lease deals included grocer **Korean Marketplace's** move to take 27,493 square feet in Kearny Mesa; the leasing of 13,280 square feet by electronics installer **Mount It** in Miramar; and **Dollar Tree's** leasing of 13,200 square feet in Chula Vista.