



Harbor Short Duration Fund



Ken O'Donnell

2nd Quarter, 2010 Commentary

"...by any measure job growth is well below what is typically expected at this point of a recovery." -Ken O'Donnell

Weak recovery appears likely to keep short-term rates at low levels

With a number of indicators pointing to a slowing pace of economic growth, short-term interest rates appear likely to remain low at least through the end of 2010, in the view of Ken O'Donnell, Portfolio Manager of the Harbor Short Duration Fund. O'Donnell notes that the strength of the recovery is dependent in part on consumer spending, which has been hurt by stubbornly high levels of unemployment.

With short-term yields near historically low levels, the Harbor Short Duration Fund continued its recent pattern of outperformance in the second quarter of 2010. The Fund returned 1.82% for the quarter, while its benchmark, the BofA Merrill Lynch 1-3 Year US Treasury Index, returned 1.16%. On a year-to-date basis, the Fund was up 4.67% versus 1.87% for the index. For the 12 months ended June 30, 2010, the Fund returned 7.62% compared with 2.69% for the benchmark.

Ken O'Donnell's comments were made in a July 15, 2010 interview. Highlights adapted from the interview appear below. All comments relate to the quarter ended June 30, 2010, unless otherwise indicated. All references to year-to-date are for the period January 1 through June 30, 2010.

INTERVIEW HIGHLIGHTS

Related markets

Risk appetites softened modestly in the second quarter in response to sovereign credit concerns in peripheral Europe. While it is difficult to draw a direct relationship between European sovereign risk and the U.S. economic recovery, we believe that globalization has resulted in an increased level of correlation in market movements in the major economies.

Anemic job growth

Although we have experienced an increase in monthly payrolls, the rate of job creation is anemic and the unemployment rate remains elevated at 9.5%. On the margin, this is not unexpected as employment tends to be a lagging indicator. But by any measure job growth is well below what is typically expected at this point of a recovery.

Investment approach

With short-term U.S. Treasury yields firmly settled into the low end of the recent trading range, we maintain a tactical underweight. Two-year U.S. Treasury notes yielding less than 1.0% are simply unattractive. From a sector perspective we continue to hold a large allocation to government securities, which is consistent with the benchmark. We have incrementally adjusted our non-government sector exposures with a reduction in non-agency mortgage-backed securities and a modest increase in corporate debentures. Despite the volatility in the fixed income market, it remains our goal to achieve a modest incremental return over the benchmark while focusing on capital preservation.

Portfolio moves

After the crisis that we endured in 2008 and 2009, many of the mortgage securities, particularly non-agency mortgage-backed securities, suffered from a significant lack of liquidity given the challenges in the housing market. We held onto these securities despite their challenges both in liquidity and pricing terms. In the last 6 to 12 months, we have seen an improvement in price levels and liquidity in this sector and have slowly reduced our exposure. We've increased our position in the corporate debt markets as a means of diversifying the Fund's exposures away from structured securities and adding additional incremental yield in bonds that we felt were particularly attractive in the front end of the yield curve.



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Markets not back to normal

We have seen improvements in liquidity from the market lows. We've seen improvements in transaction volume. But I'm not certain we can state at this point in time that we've returned to a period of normalcy in the fixed income markets. We continue to see challenges across the depth and breadth of the markets, which tend to be very skittish in response to any type of economic and/or sovereign risk around the globe.

Total Returns

As of 06/30/2010

	Three Months	One Year	Three Years	Five Years	Ten Years	Expense Ratios** Net	Gross
Harbor Short Duration Fund - INST	1.82%	7.62%	2.51%	3.20%	3.43%	0.40%	0.49%
BofA Merrill Lynch 1-3 Year US Treasury Index	1.16%	2.69%	4.78%	4.24%	4.37%		

As of 06/30/2010, the Harbor Short Duration Fund had invested the following percentages of its assets in the sectors listed: U.S. Government Obligations, 42.30%; Mortgage Pass-through, 27.12%; Corporate Bonds & Notes, 9.14%; Asset-backed Securities, 7.66%; Collateralized Mortgage Obligations, 2.18%;

Performance data shown represents past performance, which is no guarantee of future results. Current performance may be higher or lower than the performance data shown. Investment returns and the value of an investment will fluctuate, and an investor's shares, when sold, may be worth more or less than their original cost. You can obtain performance data current to the most recent month-end (available within seven business days after the most recent month-end) by calling 800-422-1050 or visiting www.harborfunds.com.

Investors should consider the Fund's investment objective, risks, fees and expenses carefully before investing. For this and other important information, please obtain a Harbor Funds prospectus by calling 800-422-1050 or visiting www.harborfunds.com and read it carefully before investing.

The Harbor Funds performance shown assumes the reinvestment of dividend and capital gain distributions and is net of management fees and expenses. Returns for periods less than one year are not annualized. From time to time, certain fees and/or expenses have been voluntarily waived, which has resulted in higher returns. Without these waivers, the returns would have been lower. Voluntary waivers may be applied or discontinued at any time without notice. The Harbor Funds are no-load; other fees and expenses do apply to a continued investment in the Funds and are described in each Fund's current prospectus.

***About Expense Ratios: All mutual funds have expense ratios which represent what shareholders pay for operating expenses and management fees. Expense ratios are expressed as an annualized percentage of a fund's average net assets paid out in expenses. Net expense ratios reflect adjustments due to voluntary or contractual fee waivers or expense reimbursements. Expense ratio information is as of the Fund's current prospectus, as revised and supplemented from time to time. The net expense ratio for this Fund reflects a voluntary fee waiver which may be discontinued at any time without notice, although the adviser has no present intention to do so.*

Performance figures discussed in any of the Manager Commentaries reflect that of the Institutional Class shares.

This information should not be considered as a recommendation to purchase or sell a particular security and the holdings or sectors mentioned may change at any time and may not represent current or future investments.

Fixed income investments are affected by interest rate changes and the creditworthiness of the issues held by the Fund. A rise in interest rates will cause a decrease in the value of fixed income securities. Such an event would have an adverse effect on the Fund. The use of derivative instruments may add additional risk. There may be a greater risk that the Fund could lose money due to prepayment and extension risks because the Fund invests heavily at times in mortgage-related and/or asset backed securities. The Fund may engage in active and frequent trading to achieve its principal investment strategies.

The BofA Merrill Lynch 1-3 Year US Treasury Index is an unmanaged index consisting of all public U.S. Treasury obligations having maturities from 1 to 2.99 years and reflects total return. This unmanaged index does not reflect fees and expenses and is not available for direct investment.

The views expressed herein are those of the portfolio managers at the time of the interview and may not be reflective of their current opinions or future actions. These views are not necessarily those of the fund company and should not be construed as such.

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