



Harbor Unconstrained Bond Fund



Chris Dialynas

4th Quarter, 2011 Commentary

"The outlook is particularly weak in Europe, where we expect a recession of 1% to 1.5% over the course of 2012." -PIMCO Investment Strategy Group

Defensive strategies reflect conservative economic outlook for 2012

The Harbor Unconstrained Bond Fund registered returns of 0.47% for the fourth quarter and 1.32% for the 12 months ended December 31, 2011. By comparison, the BofA Merrill Lynch US Dollar 3-Month LIBOR Constant Maturity Index returned 0.07% for the quarter and 0.27% for the full year. The Harbor Unconstrained Bond Fund is managed by Chris Dialynas, a managing director of Pacific Investment Management Company (PIMCO).

A number of strategies contributed to Fund performance in the fourth quarter, PIMCO reports. These included exposure to non-U.S. government debt, emerging markets investments in Brazil and Mexico, corporate securities in the Financials and Industrials sectors, and modest investments in municipal bonds and inflation-linked bonds. A duration hedging strategy, implemented primarily through interest rate swaps in core Europe and Japan, detracted from performance.

Looking ahead, the PIMCO team expects positive but anemic economic growth in the U.S., a slowing rate of growth in China, and a possible recession in Europe in 2012. Consequently, portfolio strategies reflect a focus on sources of low-risk incremental yield versus like-duration U.S. Treasuries.

PIMCO's comments were made in a January 18, 2012, interview. Highlights adapted from the interview appear below. All comments relate to the quarter ended December 31, 2011, unless otherwise indicated. All references to year-to-date are for the period January 1 through December 31, 2011.

INTERVIEW HIGHLIGHTS

Slower growth for China

As we look around the world for growth, we do see higher growth in the emerging world, particularly in China. We don't expect China to be immune from the slowing growth rates of its major developed market customers. So to the extent that we see China's growth rates slowing, we're thinking it will slow to about 7%.

Duration strategy

We will probably be in the two-to-three-year duration area to start, with the idea being that is where we will get the maximum yield from the steepest part of the yield curve relative to volatility. What that implies is that we think there is a sweet spot of yield per unit of volatility. The Fund can get much more defensive or much more aggressive depending on what happens in the market, but that's where we'll probably start the quarter.

Weak outlook for Europe

The outlook is particularly weak in Europe, where we expect a recession of 1% to 1.5% over the course of 2012. Despite significant moves by the European Central Bank to help boost liquidity in the eurozone, we think there is a meaningful risk to the sovereign nations that are deeply in debt. Some of this has already been priced in but liquidity risks can increase, meaning that the liquidity premium can also increase.

Strong fundamentals

Looking at corporate bonds, we think U.S. companies in the Financials sector have very strong fundamentals. Their creditworthiness continues to improve and we think they're well positioned to recover from their underperformance in 2011.



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Total Returns

As of 12/31/2011

	Three Months	One Year	Three Years	Five Years	Since Inception (04/01/2010)	Expense Ratios Net	Expense Ratios Gross
Harbor Unconstrained Bond Fund - INST	0.47%	1.32%	N/A	N/A	2.34%	1.05%	5.60%
BofA Merrill Lynch US Dollar 3-Month LIBOR Constant Maturity	0.07%	0.27%	N/A	N/A	0.32%		
Barclays Capital U.S. Aggregate Bond Index	1.12%	7.84%	N/A	N/A	7.16%		

As of 12/31/2011, the Harbor Unconstrained Bond Fund had invested the following percentages of its assets in the sectors listed: U.S. Government Obligations, 41.35%; Mortgage Pass-through, 26.41%; Corporate Bonds & Notes, 16.87%; Foreign Government Obligations, 10.14%; Asset-backed Securities, 5.96%; Collateralized Mortgage Obligations, 5.83%; Bank Loan Obligations, 4.47%; Convertible Bonds, 2.46%; Municipal Bonds, 2.24%; Options, 0.23%; Convertible Preferred Stocks, 0.02%;

Performance data shown represents past performance, which is no guarantee of future results. Current performance may be higher or lower than the past 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 carefully consider the Fund's investment objectives, risks, charges and expenses before investing. To obtain a summary prospectus or prospectus for this and other information about the Fund, visit harborfunds.com or call 800-422-1050. 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.

Employing an unconstrained investment approach, the Fund may be exposed to certain types of securities, credit qualities, maturities, countries and regions not reflected in other fixed income indices. For example, high-yield, or below investment grade, securities carry a higher degree of credit risk, and may be speculative and more volatile. Investing in emerging markets may entail risk due to foreign economic and political developments. Also, foreign currency exposure can entail significant volatility, and this may be amplified with the currencies of developing countries. As a result, investors considering an investment in the Fund should be prepared to accept significant volatility in the Fund's performance, particularly over shorter time periods, due to the unconstrained nature of the Fund's investment approach.

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 reflected is contractual until 02/29/2012.

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.

The BofA Merrill Lynch US Dollar 3-Month LIBOR Constant Maturity Index tracks the performance of a synthetic asset paying Libor to a stated maturity. The index is based on the assumed purchase at par of a synthetic instrument having exactly its stated maturity and with a coupon equal to that day's fixing rate. That issue is assumed to be sold the following business day (priced at a yield equal to the current day fixing rate) and rolled into a new instrument. Barclays Capital U.S. Aggregate Bond Index is an unmanaged index of investment-grade fixed-rate debt issues with maturities of at least one year. These unmanaged indices do not reflect fees and expenses and are 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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