Harbor Capital Appreciation Fund

Manager Commentary
As of 12/31/2018

Subadviser: Jennison Associates LLC *(Since 05/01/1990)*
Portfolio Managers: Spiros "Sig" Segalas, Kathleen A. McCarragher

4th Quarter, 2018

"Entering 2019, we believe the U.S. economy remains on sound footing. Underlying interest rates and the subdued inflationary backdrop suggest the Federal Reserve is achieving its targeted goals."

Jennison Associates LLC

Economic Overview

During the fourth quarter of 2018, an equity market selloff reflected mounting investor concerns about a range of issues, including the pace of U.S. growth, decelerating expansion in non-U.S. economies, U.S. interest rate increases and their effect on U.S. economic growth, the rising risk of a major trade war between the U.S. and China, and the state of U.S. trade alliances with other major trading partners. In addition, discord and uncertainty about domestic policy culminated in a partial U.S. government shutdown as the year drew to a close. Algorithmic computer trading and passive investment vehicles that use technology-based, dynamic, factor-weighted models amplified the declines.

Market weakness came even as the U.S. economy showed continued strength. Employment was solid, with the unemployment rate near a record low. Wages continued to rise, inflation remained subdued (aided by a substantial decline in the price of crude oil during the quarter), and retail sales ended the holiday period on a robust note. The market's drop and policy uncertainty, however, took a toll on consumer confidence, and several purchasing managers surveys showed weakening trends. The U.S. Federal Reserve (the Fed) continued to modestly and gradually increase the federal funds target rate. In reducing its outlook for rate increases in 2019 from three to two, the Fed acknowledged the prospect of slowing growth. Strikes and protests in France, changing political leadership in Germany, unresolved and contentious Brexit negotiations in the U.K., and slowing growth in China added to concerns about the state of global growth heading into 2019.

Portfolio Review

In the fourth quarter of 2018, the Harbor Capital Appreciation Fund (Institutional Class) returned -16.40%, underperforming its benchmark, the Russell 1000® Growth Index, which returned -15.89%.

On balance, stock selection was positive during the quarter, while sector allocation effects were negative. Consumer Staples detracted from relative performance, due to an underweight position and stock selection. Stock selection in Health Care and Communication Services also hindered relative results. In contrast, Information Technology and Consumer Discretionary contributed to relative performance, due to security selection.

Individual detractors from performance included Information Technology holding NVIDIA Corporation. The graphics chipmaker is strong in key high-growth markets where developers have coalesced around the company's architecture and platform. After strong performance in the prior 18 months, the shares fell significantly during the fourth quarter, reflecting low- and mid-end gaming graphics processing unit inventory issues that were exacerbated by a slowdown in the cryptocurrency mining boom. Apple, Inc., also detracted from performance in Information Technology. Apple's decline came as management's decision to discontinue reporting unit sales coincided with weakening order trends in provider channels.

In Consumer Discretionary, Amazon.com, Inc., hindered results. The company's shares declined amid an unfavorable reaction to its revenue and earnings outlook.

Conversely, contributors to performance included Red Hat, Inc., in Information Technology. The company is the market-leading vendor of Linux, an open-source computer operating system, and its shares advanced sharply on news that International Business Machines Corporation plans to buy Red Hat. Workday, Inc., also boosted results in Information Technology. The company's technological advantage in cloud-based enterprise applications for financial and human resources operations has continued to drive share gains in large existing markets.

In Consumer Discretionary, shares of Tesla, Inc., rose as production levels exceeded expectations and Model 3 production hit the company's 5,000 per week target, which helped quell controversy surrounding Chief Executive Officer Elon Musk.

Over the course of 2018, exposures to Consumer Staples and Industrials declined, while the weight in Health Care increased. As of December 31, 2018, the Fund's largest overweight was Consumer Discretionary, and its largest underweight was Industrials. Several indexes made meaningful changes to sectors, effective as of the close of business on September 28, 2018. The changes reclassified several Fund holdings and effectively lowered the Fund's weight in Information Technology and increased its weight in Telecommunication Services, which was renamed Communication Services.

We believe the market's focus on company fundamentals through much of 2018 favored the Fund's investment approach, although investor concerns about trade wars contributed to volatility in some holdings. Increased market volatility and risk aversion in the fourth quarter were detrimental to companies with projected high earnings growth, like those held in the Fund, regardless of their underlying fundamentals. By identifying what we believe are fundamentally strong companies through our disciplined, research-intensive approach, we believe we have constructed a portfolio that is positioned to generate above-average returns over the longer term. We believe that the market will, as it has historically, value them appropriately over the long-term.

Outlook

Market enthusiasm in most of 2018, spurred by the biggest reduction in corporate tax rates in U.S. history, has been dampened by multiple concerns, including the unconventional style and unsettling initiatives of the White House, global trade conflict, signs of economic weakness in some of the world's largest economies, and moderating U.S. corporate profit growth. Entering 2019, we believe the U.S. economy remains on sound footing. Underlying interest rates and the subdued inflationary backdrop suggest the Fed is achieving its targeted goals. Wages appear headed for continued modest growth, reflecting the strength of the U.S. labor market and the low unemployment rate. While housing and automobile sales peaked in 2017, overall consumer spending has continued to grow, although at a more moderate pace.

Our focus on companies with distinct competitive advantages and strong earnings growth has historically led to attractive returns over the long-term. Despite short-term headwinds, we have every confidence that our approach will continue to be validated as investors refocus on fundamentals.

Harbor Funds

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ECONOMIC SECTORS

	% of Net Assets
Information Technology	33.50
Consumer Discretionary	20.70
Communication Services	16.43
Health Care	13.71
Industrials	5.36
Financials	3.84
Consumer Staples	3.27
Real Estate	1.49
Materials	0.86
Energy	0.47

TOP TEN HOLDINGS

Company Name	% of Net Assets
1. Amazon.com Inc.	5.75
2. Microsoft Corp.	5.12
3. MasterCard Inc.	3.82
4. Salesforce.com Inc.	3.78
5. Tencent Holdings Ltd.	3.55
6. VISA Inc.	3.48
7. Boeing Co.	3.33
8. Apple Inc.	3.24
9. NetFlix Inc.	3.21
10. Alphabet Inc. Class A	2.98

ADDITIONAL HOLDINGS

Company Name	% of Net Assets
Tesla Inc.	2.31
NVIDIA Corp.	1.50
Workday Inc.	1.49
Red Hat Inc.	1.11

TOTAL RETURNS

	Three Months	1 Yr.	5 Yr.	10 Yr.	Since Incp. (12/29/1987)	Expense Ratios Net	Expense Ratios Gross
Harbor Capital Appreciation Fund - *INST*	-16.40%	-1.03%	10.29%	15.27%	11.33%	0.66%	0.71%
Russell 1000® Growth Index	-15.89%	-1.51%	10.40%	15.29%	10.03%		
S&P 500 Index	-13.52%	-4.38%	8.49%	13.12%	10.17%		

Performance data shown represents past performance and is no guarantee of future results. Past performance is net of management fees and expenses and reflects reinvested dividends and distributions. Past performance reflects the beneficial effect of any expense waivers or reimbursements, without which returns would have been lower. Investment returns and principal value will fluctuate and when redeemed may be worth more or less than their original cost. Returns for periods less than one year are not annualized. Current performance may be higher or lower and is available through the most recent month end at harborfunds.com or by calling 800-422-1050.

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

Expense ratio information is as of the Fund's current prospectus, as supplemented. Gross expenses are the Fund's total annual operating expenses. The net expense ratios for this fund are subject to a contractual management fee waiver through 02/28/2019.

The Russell 1000® Growth Index is an unmanaged index generally representative of the U.S. market for larger capitalization growth stocks. The Standard & Poor's 500 Index is an unmanaged index generally representative of the U.S. stock market. These unmanaged indices do not reflect fees and expenses and are not available for direct investment. The Russell 1000® Growth Index and Russell® are trademarks of Frank Russell Company.

Since the Fund may hold foreign securities, it may be subject to greater risks than funds invested only in the U.S. These risks are more severe for securities of issuers in emerging market regions. At times, a growth investing style may be out of favor with investors which could cause growth securities to underperform value or other equity securities.

Stock markets are volatile and equity values can decline significantly in response to adverse issuer, political, regulatory, market and economic conditions.

Views expressed herein are drawn from commentary provided to Harbor by the subadviser, Jennison Associates LLC, and may not be reflective of their current opinions or future actions, are subject to change without prior notice, and should not be considered investment advice.

Investors should carefully consider the investment objectives, risks, charges and expenses of a Harbor fund before investing. A summary prospectus or prospectus for this and other information is available at harborfunds.com or by calling 800-422-1050. Read it carefully before investing.

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