Harbor Emerging Markets Equity Fund

Manager Commentary
As of 06/30/2019

Subadviser: Oaktree Capital Management, L.P. *(Since 11/01/2013)*
Portfolio Managers: Frank J. Carroll, Timothy D. Jensen

2nd Quarter, 2019

"Consistent with our fundamental approach, we try to construct the Fund based on bottom-up research rather than top-down decisions based on macro-level events."

Oaktree Capital Management, L.P.

Market in Review

There were two significant macroeconomic events during the second quarter of 2019: the escalation of the U.S.-China trade war and the increasingly dovish stance of the U.S. Federal Reserve (Fed). Trade negotiations between the U.S. and China have been underway for more than a year, and sentiment towards Chinese stocks—and, more generally, Asian stocks—has shifted with developments in the negotiations. In December 2018, President Trump and President Xi met at the G-20 summit and agreed to defer new tariffs and work towards an agreement. Chinese equities rallied sharply until late April. In early May, Trump announced that negotiations had faltered. He imposed higher tariffs on a large tranche of Chinese exports, and markets sold off sharply. In June, negotiations resumed, and at quarter end Trump and Xi agreed to work towards a trade deal, with Trump deferring tariffs on the remainder of Chinese exports. Resolution of the trade dispute would provide a better market backdrop.

The Fed has become progressively more dovish during the first half of the year in response to softer economic data and trade-related uncertainty. Fed leadership has suggested an interest rate cut may happen as soon as July. U.S. and global interest rates have declined significantly. Lower risk-free rates have supported equity markets.

Portfolio Performance

In the second quarter of 2019, the Harbor Emerging Markets Equity Fund (Institutional Class) returned 1.59%, outperforming its benchmark, the MSCI Emerging Markets (ND) Index, which returned 0.61%.

The Fund's relative outperformance was largely driven by positive stock selection in China, which more than offset the negative effect of our overweight allocation there. Stock selection in South Africa and Greece also helped, along with our overweight allocation to Russia. Stock selection in Russia detracted. By sector, stock selection among Financials, Consumer Staples, and Materials helped drive performance, while selection among Energy stocks had a negative impact. Our overweight exposure to Financials contributed positively.

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.

The views expressed herein may not be reflective of current opinions, are subject to change without prior notice, and should not be considered investment advice.

Consistent with our fundamental approach, we try to construct the Fund using bottom-up research rather than top-down decisions based on macro-level events. We shifted our positioning marginally during the quarter, reducing Chinese exposure in March and adding some back in June. The Fund maintains its value bias, and we believe that there are more opportunities in value names than in growth names in emerging markets.

Contributors and Detractors

Our three largest contributors to relative performance during the quarter were Anglogold Ashanti, Sberbank of Russia, and Alpha Bank. Anglogold Ashanti rallied as gold prices rose amid easier monetary policy. In our view, Anglogold has been streamlining its mining portfolio and repairing its balance sheet over the past few years, leaving it well-placed for a better pricing environment. Sberbank continues to execute very well, reporting better-than-expected earnings and return on equity. The Russian market has performed well year-to-date. Alpha Bank was priced near distressed levels and has benefited from improving Gross Domestic Product (GDP) growth and falling interest rates in Greece, as well as anticipation of a parliamentary election, which was won by the more market-friendly political party.

Our largest detractors during the quarter were Weibo, Indiabulls Housing Finance, and Semen Indonesia. Weibo is a Chinese social media company that performed poorly due to slower-than-expected advertising growth. Indiabulls Housing Finance has been a poor performer for several quarters due to dislocations in the funding market after the failure of an unrelated non-bank financial company in India in late 2018. Semen Indonesia pulled back during the quarter after several quarters of strong performance.

Buys and Sells

We added a position in MTN Group during the quarter. MTN is a mobile phone operator headquartered in South Africa, and active in more than 20 countries in Africa and the Middle East. The company’s largest market is Nigeria, where it is the largest cellular phone operator. MTN is the largest or second-largest operator in almost all of its markets. The company endured five years of difficult relative performance due to weak economic growth in several of its major markets, regulatory issues and a weak balance sheet. We added the name because, in our view, the new management team has focused on balance sheet repair, the regulatory issues have been addressed, Nigeria and a few other key markets are experiencing stronger growth, and MTN launched mobile financial services, which we see as an attractive opportunity for incremental growth and profitability.

Yum China performed poorly during the escalation of the trade war in May. During past periods of tensions between China and other countries, we have seen propaganda against other nations (such as Japan and South Korea) on traditional media and social media affect sales of companies from those nations. The Chinese government has kept a tight lid on anti-American propaganda for most of the past year, but when social media posts started to appear against U.S. brands in May, we exited Yum China.

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Country Allocation

At the country level, we continue to maintain a sizeable overweight to China, with smaller overweight allocations to Brazil and Russia. At quarter end, our largest overweights by country were China, Brazil, Russia, and Indonesia. We remain underweight Taiwan and have no exposure to Turkey, Malaysia, or Argentina.

Our style is not heavily thematic, but we are willing to tilt the Fund's portfolio when prices change and news flow shifts. As mentioned above, we reduced our China overweight in late March/early April on price, but added back to China at lower prices in late May/early June. We shifted out of some potentially vulnerable names, including Yum China, but replaced them with two Chinese consumer durable companies, Suofeiya Home Collection and Geely Automobile Holdings. We also added an Information Technology company, Hangzhou Hikvision Digital Technology, and a gaming platform, Huya, and several small health care names. Our Chinese exposure became more focused on domestic developments. We also added to our Brazil exposure after the market corrected.

Outlook

We have a constructive view of the market going forward, and will likely be even more bullish if U.S.-China trade negotiations conclude successfully. We continue to believe that it is in everyone's interest to maintain an open global trading system, although we would expect some long-term diversification of sourcing away from China and recurring limitations on trade in equipment that is sensitive to national security. The easing of monetary policy appears to be a global trend; a number of emerging markets have high real interest rates and, in our view, are likely to reduce rates. We believe this could be supportive of lower discount rates. At a country level, most of the recent national elections—such as India, South Africa, and Indonesia—have been won by the market-friendly party, and Brazil is making good progress on its economic reform agenda. We are very pleased with the improvements we have seen in capital allocation and corporate governance among a growing number of leading emerging markets companies. Finally, valuations are attractive in absolute terms and relative to developed markets.

Harbor Funds

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ECONOMIC SECTORS

	% of Net Assets
Financials	26.32
Energy	14.96
Information Technology	13.93
Communication Services	10.40
Materials	8.96
Consumer Staples	8.47
Consumer Discretionary	6.29
Industrials	3.68
Health Care	2.48
Real Estate	2.33
Utilities	0.75

TOP TEN HOLDINGS

Company Name	% of Net Assets
1. Tencent Holdings Ltd.	6.86
2. Samsung Electronics Co. Ltd.	5.45
3. Taiwan Semiconductor Manufacturing Co	3.83
4. Ping An Insurance Group Co. of China	3.38
5. LUKOIL Pjsc ADR	3.21
6. China Construction Bank Corp.	3.20
7. ICICI Bank Ltd. ADR	2.88
8. Petroleo Brasileiro SA ADR	2.59
9. Sberbank of Russia PJSC ADR	2.52
10. Itau Unibanco Holding SA ADR	2.19

ADDITIONAL HOLDINGS

Company Name	% of Net Assets
AngloGold Ashanti Ltd. ADR	1.84
MTN Group Ltd.	1.48
Semen Indonesia Persero Tbk PT	1.23
Alpha Bank AE	1.13
Geely Automobile Holdings Ltd.	0.92
Weibo Corp. ADR	0.80
Indiabulls Housing Finance Ltd.	0.71
Suofeiya Home Collection Co. Ltd.	0.54
Hangzhou Hikvision Digital Technology Co	0.52
Huya Inc. ADR	0.48
Yum China Holdings Inc.	0.00

TOTAL RETURNS

	Three Months	1 Yr.	5 Yr.	10 Yr.	Since Incp. (11/01/2013)	Expense Ratios Net	Expense Ratios Gross
Harbor Emerging Markets Equity Fund - *INST*	1.59%	7.17%	1.74%	N/A	2.26%	1.16%	1.35%
MSCI Emerging Markets (ND) Index	0.61%	1.21%	2.49%	N/A	2.74%		

TOP TEN COUNTRIES

Country	% of Net Assets
China	39.72
South Korea	11.94
Brazil	9.80
India	9.04
Russia	6.50
South Africa	6.35
Taiwan	5.41
Indonesia	3.12
Thailand	2.31
Mexico	2.07

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This information should not be considered as a recommendation to purchase or sell a particular security. The holdings or countries 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 an expense limitation agreement, excluding interest expense, if any, through 02/29/2020.

The MSCI Emerging Markets (ND) Index is a market capitalization weighted index of equity securities in more than 20 emerging market economies. This unmanaged index does not reflect fees and expenses and is not available for direct investment.

Investing in international and emerging markets poses special risks, including potentially greater price volatility due to social, political and economic factors, as well as currency exchange rate fluctuations. These risks are more severe for securities of issuers in emerging market regions. Stocks of small and mid cap companies pose special risks, including possible illiquidity and greater price volatility than stocks of larger, more established companies.

At times, a value investing style may be out of favor with investors which could cause value securities to underperform growth 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, Oaktree Capital Management, L.P., 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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