Harbor High-Yield Bond Fund

Manager Commentary
As of 12/31/2018

Subadviser: Shenkman Capital Management, Inc. *(Since 12/01/2002)*
Portfolio Managers: Mark R. Shenkman, Justin W. Slatky, Eric Dobbin, Steven N. Schweitzer, Robert S. Kricheff, Neil Wechsler, CFA

4th Quarter, 2018

"While volatility appears likely to remain elevated, we view a moderation of growth, as opposed to a reversal of growth, as the most likely scenario, and we plan to maintain our conservative positioning."

Shenkman Capital Management, Inc.

Economic Overview

Financial markets were roiled in the final quarter of 2018 by a number of factors: ongoing fears that the looming US-China trade war could hamper global economic growth, plummeting crude oil prices, President Trump's recurring attacks on the Federal Reserve, a retrenchment in equities, anxiety over the Fed's rate tightening trajectory, and the pace of securities rolling off of the Fed's balance sheet. The ICE BofAML U.S. High Yield Index (H0A0) sank 4.67% in the fourth quarter, its worst quarterly decline since the third quarter of 2015, when the oil price crash shook markets. Triple-C rated credits came under particular pressure, falling 10.35% and leaving the category with a quarter-ending yield-to-worst greater than 1,100 basis points (bps) over Treasuries. Single-B rated bonds fared better, with a -4.85% return, while double-B's declined by 2.99% as "risk-off" sentiment and rallying Treasuries buoyed the rating classification. Index prices plummeted $6.21 to $92.31, pushing the yield-to-worst higher by 167 bps to 7.95%, and the spread- to-worst wider by 199 bps to +537bps. Yield and spread now represent their highest levels since mid-2016.

The trailing par-weighted default rate maintained its downward trend, falling to 1.81%, off from 2.02% at the end of September and lower by nearly 50% from 3.57% at the end of 2016. Only $3.35 billion of bonds defaulted in the quarter. The trailing default rate continues to be inflated by the February 2018 bankruptcy of iHeart Communications and would total just 1.08% if this widely anticipated default were removed from the calculation. Due to elevated market volatility, high yield bond new issuance fell precipitously year-over-year, to just $6.1 billion versus $72.5 billion in 2017's fourth quarter. Investors withdrew $14.2 billion from high yield mutual funds in the fourth quarter of 2018, compared to $20.7 billion in outflow for all of 2017.

Portfolio Review

In the 4th quarter of 2018, the Harbor High Yield Bond Fund (Institutional Class) returned -4.23%, while its benchmark, the ICE BofAML U.S. Non-Distressed High Yield Index (H0ND), returned -4.07%. Negative selection in Oil and Gas (partly due to survivorship bias in the index) and negative selection and underweight in Finance: Banking detracted from performance, while positive selection in Utilities: Gas and Finance: Services contributed to performance. Underweight in BB rated credits and negative selection in CCC-rated credits detracted from performance; positive selection in B-rated credits helped performance. Additionally, the Fund's out-of-index allocation to bank loans was also a contributor for the quarter.

Sanchez Energy Corporation, Weatherford International Ltd., and Transocean Guardian Ltd. detracted from relative performance during the quarter. These credit structures declined significantly as oil prices decreased. Frontier Communications Corporation and DISH DBS Corporation bonds fell as both companies continued a trend of weaker earnings.

Conversely, Calpine Corporation contributed to relative results, as the steadiness of the company's utility business led investors to hold the bonds during a more volatile period. Tesla Inc. also helped results as the company's earnings exceeded investor expectations. Wrangler Buyer Corporation helped results, as GFL Environmental Inc. acquired the company and the bonds rallied when they were tendered. Trinidad Drilling Ltd. and LSC Communications Inc. were both the subject of takeover bids and their bonds rallied significantly because the buyers are tendering for the bonds.

Outlook

Although the magnitude of financial market nervousness accelerated during the quarter as concerns over global economic health and worries about the outlook for additional interest rate hikes intensified, we believe the level of "doom and gloom" in the high yield market may have overshot to the downside. In our view, the U.S. economy appears poised to generate gross domestic product in excess of 2%. With Fed Chair Jerome Powell signaling a less aggressive rate-hike path in 2019 amid tepid inflation, concerns of a near-term U.S. recession could be alleviated despite slower worldwide growth. Additionally, we continue to believe we could see an elongated period of below-average default activity, as the past few years' record pace of refinancing across loans and bonds has left balance sheets in excellent shape, in our view. Meanwhile, we believe strong labor markets and robust income growth of more than 3% could remain supportive of consumer consumption levels. From a technical standpoint, we believe the lightest new issuance since 2009, a healthy yield approaching 8% and a spread-to-worst in the mid-500 basis point range appear compelling for investors seeking income. While volatility appears likely to remain elevated, we view a moderation of growth, as opposed to a reversal of growth, as the most likely scenario, and we plan to maintain our conservative positioning.

Harbor Funds

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ECONOMIC SECTORS

	% of Net Assets
Communication Services	21.85
Energy	12.98
Health Care	11.62
Consumer Discretionary	9.44
Industrials	9.28
Materials	8.37
Financials	6.97
Information Technology	6.88
Real Estate	5.82
Consumer Staples	3.39
Utilities	3.28

TOP TEN HOLDINGS

Company Name	% of Net Assets
1. CSC Holdings LLC	0.71
2. Unit Corp.	0.71
3. AMC Networks Inc.	0.70
4. CCO Holdings LLC	0.69
5. Range Resources Corp.	0.63
6. Sirius XM Radio Inc.	0.62
7. GCI Inc.	0.62
8. Vistra Energy Corp.	0.58
9. Nationstar Mortgage LLC	0.57
10. Hughes Satellite Systems Corp.	0.56

ADDITIONAL HOLDINGS

Company Name	% of Net Assets
Dish DBS Corp.	0.42
Trinidad Drilling Ltd.	0.37
Tesla Inc.	0.31
Sanchez Energy Corp.	0.26
Gfl Environmental Inc.	0.24
Calpine Corp.	0.21
Weatherford International Ltd.	0.14
LSC Communications Inc.	0.10
Frontier Communications Corp.	0.05
Transocean Guardian Ltd.	0.01
Wrangler Buyer Corp.	0.00

TOTAL RETURNS

	Three Months	1 Yr.	5 Yr.	10 Yr.	Since Incp. (12/01/2002)	Expense Ratios Net	Expense Ratios Gross
Harbor High-Yield Bond Fund - *INST*	-4.23%	-2.21%	2.89%	7.66%	6.46%	0.63%	0.72%
ICE BofAML US Non-Distressed High Yield Index	-4.07%	-2.01%	4.04%	8.93%	7.14%		
ICE BofAML US High Yield Index (H0A0)	-4.67%	-2.25%	3.82%	10.99%	8.16%		

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 countries mentioned may change at any time and may not represent current or future investments.

The Fund charges a redemption fee of 1.00% on redemption of shares that are held for less than 90 days.

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 02/29/2020.

The ICE BofAML US Non-Distressed High Yield Index is a subset of the ICE BofAML US High Yield Index (H0A0) including all securities with an option-adjusted spread less than 1,000 basis points. The ICE BofAML US High Yield Index (H0A0) is an unmanaged index that tracks the performance of below investment grade U.S. Dollar-denominated corporate bonds publicly issued in the U.S. domestic market. All bonds are U.S. Dollar-denominated and rated Split BBB and below. These unmanaged indices do not reflect fees and expenses and are not available for direct investment.

Fixed income investments are affected by interest rate changes and the creditworthiness of the issues held by the Fund. As interest rates rise, the values of fixed income securities held by the Fund are likely to decrease and reduce the value of the Fund's portfolio. High yield investing poses additional credit risk related to lower-rated bonds.

Views expressed herein are drawn from commentary provided to Harbor by the subadviser, Shenkman Capital Management, Inc., 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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