Harbor International Fund

Manager Commentary
As of 03/31/2019

Subadviser: Marathon Asset Management LLP *(Since 08/22/2018)*
Portfolio Managers: Neil M. Ostrer, Charles Carter, Nick Longhurst, William J. Arah, Simon Somerville, Michael Nickson, CFA, Michael Godfrey, CFA, David Cull, CFA

1st Quarter, 2019

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Marathon Asset Management LLP (Marathon-London)

Economic Overview

Following central bank efforts to "normalize" monetary policy by raising rates in the latter part of 2018, the U.S. Federal Reserve (Fed) became more dovish in the first quarter of 2019, as did the European Central Bank, by more or less committing to no further interest rate hikes. Trade negotiations between the U.S. and China seemingly moved closer to culmination as enforcement issues appear to have largely been addressed and U.S. tariff hikes on China have been suspended. That said, sticking points in the negotiations clearly remain.

In addition, after an initial delay, the deadline for Britain's exit from the European Union has been deferred (once again!) to October 31, 2019, which has ruled out the imminent possibility of a hard or "no deal" Brexit. Collectively, these developments seem to have eased market sentiment and resulted in global equity markets rallying sharply, reversing course from the tail end of last year.

Portfolio Review

In the first quarter of 2019, the Harbor International Fund (Institutional Class) returned 9.75%, performing in line with its benchmark, the MSCI EAFE (ND) Index, which returned 9.98%.

A positive contribution from currency exposure was offset by a negative allocation effect, while the overall contribution from stock selection was negligible. The largest positive influences in the Fund during the period came from stock selection within the limited out-of-benchmark allocation to emerging markets (particularly China and Taiwan), stock selection within Denmark and Sweden, and an overweight to the rising British Pound Sterling. Notably, the currency allocation is a residual of individual stock decisions, as we do not actively manage currency exposure. Conversely, the Fund's underweight exposure to, and stock selection within, the Pacific ex-Japan region exerted one of the largest negative influences on relative returns, as did the Fund's residual cash exposure.

From a sector allocation standpoint, the Fund's overweight exposure to the underperforming Communication Services sector and underweight exposure to the strong-performing Real Estate sector weighed on relative returns. Conversely, the Fund's underweight exposure to the Financials sector, which lagged the broader index return, contributed positively to relative performance.

Top individual contributors included Assa Abloy, GN Store Nord, and Rightmove. Lock manufacturer Assa Abloy rallied sharply after reporting a surprisingly robust organic growth figure for the fourth quarter. Shares of GN Store Nord jumped as the Danish medical device company reported strong fourth quarter results and higher-than-expected guidance for 2019 for both their Hearing and Audio businesses. Rightmove, the dominant online real estate listings portal in the U.K., was a positive influence as results showed that flat real estate numbers were more than offset by higher price increases.

Top individual detractors included TUI, EssilorLuxottica, and Stabilus. Tour operator group TUI issued a profit warning caused by the heatwave in Northern Europe, the grounding of the Boeing 737 MAX aircraft, and a difficult near-term outlook. The full year earnings forecast was reduced by 25%. Market structure, however, remains consolidated and rational. EssilorLuxottica exerted a negative effect as the company suffered from a clash between the two sides of their recently merged Italian and French groups, which has led to a request for arbitration. Component manufacturer Stabilus largely focused on the design and production of gas springs (the ones that control the tailgate of a car or the height of a luxury office chair) during the quarter. Dampers performed poorly due to the reduction in guidance for 2019 after reporting first quarter revenues below broker estimates.

The largest country overweights entering the year were the U.K. and Denmark. The largest underweights were France and Australia. These weights did not materially change during the quarter.

The largest sector overweights entering the year were Industrials and Consumer Discretionary. The largest underweights were Financials and Real Estate. It’s important to note that the Fund’s country and sector weights relative to the benchmark are a byproduct of our bottom-up, fundamental investment approach and opportunity set.

We initiated a position in JAFCO during the quarter. The company is Japan’s only listed venture capital firm. With a price-to-earnings multiple of 11 as well as half its market capitalization in equity and cash on the balance sheet, we believe it presents an inviting investment case. The company also has multiple investments within its own funds, aligning its interests with those of long-term shareholders.

We sold our position in investment holding company GL Limited, based in Singapore, during the period for valuation reasons.

Outlook

The inherently contrarian nature of our investment approach has made it challenging—though not impossible—to keep pace during what has been a fairly broad-based and indiscriminate ongoing rally across equity markets for several years. However, we believe the recent uptick in market volatility and increased prospects for future equity market retrenchment may present a more favorable backdrop, given the Fund’s positioning and characteristics profile. While we are taking advantage of price dislocations and establishing new, often more "cyclical" positions where relative valuations present the opportunity to do so, we remain focused on downside protection with a quality tilt.

Despite the broad-based recovery in Europe during the first quarter of 2019, there are still pockets of value to be found. There remain, however, significant nearer term uncertainties relating to Brexit as well as U.S. trade tensions with both China and now the European Union. We believe slowing economic growth out of China could have a negative impact on European businesses, which are largely export-oriented. Tempering this concern, the earnings season produced better-than-expected results. Likewise, the significant number of meetings we held with company management teams after results season were overall cautiously positive.

In the market's view, Japan can only join the macroeconomic party once policy elsewhere has "worked," kicking off a round of growing external demand while domestic demand remains demographically constrained. Despite unemployment of 2.3% amid record participation rates and chronic shortages of labor beginning to materially impact corporate behavior, this perception is deep-rooted and underlines how entrenched the belief is that Japan can "never work." Against this macro backdrop, foreigners remained heavy net sellers, while the market was still heavily influenced by passive buying from the Bank of Japan. For context, the passive share of new flows is now over 60%, compared to 40% in the U.S. and 30% in European markets.

Given current macroeconomic trends, corporate governance has increasingly moved to the foreground, and we anticipate wide ranging—and in some cases quite dramatic—initiatives to be announced at upcoming annual meetings, with a clear focus on shareholder returns, corporate structures, and balance sheet efficiency. We believe the likelihood of Japan's current stance of tight fiscal, "excessively" loose monetary policy —which is totally contrary to the route the rest of the world is starting to take—continuing indefinitely is low. Indeed, discussions are building over the desirability of raising the sales tax while the Bank of Japan is under growing pressure to explain its rationale for sticking to a policy that clearly is not working.

Despite a combination of factors weighing heavily on emerging markets last year, we believe underlying company financials remain attractive. However, in our view, slowing economic growth continues to be a risk to investors, particularly in China.

The developed Asian markets are highly influenced and reliant on China for growth. With a slowdown in the Chinese economy, higher oil prices, and sustained trade tensions between the U.S. and China, our outlook for the region has deteriorated. However, declines in valuations in 2018 have led to promising investment opportunities among select Asian exporters as well as more domestically focused stocks.

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ECONOMIC SECTORS

	% of Net Assets
Industrials	23.88
Financials	14.51
Consumer Discretionary	13.25
Consumer Staples	10.64
Health Care	9.40
Communication Services	7.87
Information Technology	6.46
Materials	6.02
Energy	3.55
Real Estate	0.59
Utilities	0.50

TOP TEN HOLDINGS

Company Name	% of Net Assets
1. Coloplast AS	1.28
2. Intertek Group plc	1.25
3. Roche Holding AG	1.23
4. Vestas Wind Systems AS	1.16
5. Compass Group plc	1.15
6. Rightmove plc	1.11
7. Assa Abloy AB Class B	1.05
8. BP plc	0.99
9. Toyota Motor Corp.	0.96
10. GN Store Nord AS	0.95

ADDITIONAL HOLDINGS

Company Name	% of Net Assets
EssilorLuxottica SA	0.63
Stabilus SA	0.29
TUI AG	0.29
Jafco Co. Ltd.	0.02
GL Ltd.	0.00

TOTAL RETURNS

	Three Months	1 Yr.	5 Yr.	10 Yr.	Since Incp. (12/29/1987)	Expense Ratios Net	Expense Ratios Gross
Harbor International Fund - *INST*	9.75%	-9.43%	-0.32%	8.59%	9.99%	0.77%	0.89%
MSCI EAFE (ND) Index	9.98%	-3.71%	2.33%	8.96%	5.17%		

TOP TEN COUNTRIES

Country	% of Net Assets
United Kingdom	25.68
Japan	23.38
France	6.09
Germany	5.57
Denmark	5.25
Switzerland	5.22
Netherlands	3.68
Australia	3.10
Sweden	2.71
South Korea	2.13

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.

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 and an expense limitation agreement, excluding interest expense, if any, through 02/29/2020.

The MSCI EAFE (ND) Index is an unmanaged index generally representative of major overseas stock markets. The MSCI All Country World Ex. US (ND) Index is a free float-adjusted market capitalization weighted index that is designed to measure equity market performance in the global developed and emerging markets, excluding the United States. These unmanaged indices do not reflect fees and expenses and are not available for direct investment.

The subadviser's assessment of the capital cycle for a particular industry or company may be incorrect. Investing in companies at inopportune phases of the capital cycle can result in the Fund purchasing company stock at pricing levels that are higher than the market dynamics would support and therefore subject the Fund to greater risk that the stock price would decline rather than increase over time.

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, Marathon Asset Management LLP (Marathon-London), 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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