Harbor International Growth Fund

Manager Commentary
As of 12/31/2018

Subadviser: Baillie Gifford Overseas Limited *(Since 05/21/2013)*
Portfolio Managers: Gerard Callahan, Iain Campbell, Joseph M. Faraday, CFA, Moritz Sitte, CFA, Sophie Earnshaw, CFA

4th Quarter, 2018

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Baillie Gifford Overseas Limited

Economic Overview

The macroeconomic commotion responsible for weak year-to-date performance as of the end of September, was again influential, rounding off a poor year for international stock markets. The MSCI ACWI ex U.S. Index lost 11.5% of its value over the quarter. Some 'highlights' of the fourth quarter were the U.K. Prime Minister Theresa May surviving a confidence vote among Conservative Members of Parliament in December, U.S. – China trade negotiations continuing, and the Federal Reserve raising interest rates again in the U.S., all of this capping a generally underwhelming year for international, as well as U.S, stock markets. What has really changed this year? The answer, we believe, is: not much. All the uncertainty in markets appears to have bred a rather pessimistic outlook among market participants, while the underlying fundamentals of many companies are unchanged, as is the case for most of the Harbor International Growth Fund's holdings. We consider one year to be a short time horizon, rarely reflective of long-term possibilities.

Portfolio Review

In the fourth quarter of 2018, Harbor International Growth Fund (Institutional Class) returned -15.17%, underperforming its benchmark, the MSCI All Country World Ex. US (ND) Index, which returned -11.46%.

Stock selection overall –particularly in Consumer Discretionary, Consumer Staples, and Communication Services – was responsible for the bulk of underperformance during the quarter. Sector allocations also detracted from relative returns, due partly to an overweight position in Consumer Discretionary, one of the worst performing index sectors for the quarter, and lack of exposure to Utilities and Real Estate, the two best performers. The Fund's sector weightings are purely a residual outcome of the bottom-up stock selection process. Positive stock selection drove contributions from Materials and Financials.

There was an eclectic mix of companies in the Fund whose performance fared better than that of the wider market in the fourth quarter and, more broadly, 2018. At the top of the list for the quarter were two India-based companies: the banking corporation Housing Development Finance Corp (HDFC) and paint manufacturer Asian Paints. HDFC is a relatively recent purchase that, in our view, has performed satisfactorily so far. Asian Paints has seen double-digit volume growth in recent periods and has shown strong pricing power. As a company reliant on crude oil in its manufacturing processes, a weakening oil price was also helpful, and it was pleasing to see the share price reflecting this.

For the year 2018, the top contributors were Japanese cosmetics business Shiseido and Auto Trader, the online car sales platform in the United Kingdom. Shiseido's strong performance followed its focus on a smaller number of brands within its stable and the company's targeting of the travel retail segment. Chinese travelers in particular boosted Shiseido's revenues, and although the shares declined from earlier highs, they still outperformed the market overall. Auto Trader saw a recovery in its share price over the year as the company made modest upgrades to its profit forecasts. The business appeared to defy pessimism around the domestic backdrop amid Brexit uncertainty, as well as fear over new competition, to deliver steady growth throughout the year despite car sales in the U.K. being relatively subdued.

The largest detractors for the quarter were ASOS, a British online fashion retailer, and the Swedish music-streaming business Spotify. ASOS released a profit warning in the final quarter of the year that represented a significant downgrade from previous levels. The online clothing sales space experienced widespread struggles in performance terms. ASOS suffered from increasing competition in this sector, with deep discounts eating into the company's profit margins. Zalando, the German online clothing retailer and another top detractor for the quarter, has had a similarly difficult time. In its case, the issue was exacerbated by a couple of operational blunders. We still believe these businesses are well placed to grow in the long-term and have been pleased to see continued investment by these companies in their operations. ASOS and Zalando were the two largest detractors from relative performance for the full year. In the fourth quarter, Spotify found itself on the receiving end of concerns over the demand for its product and how differentiated it is in a market where there are other platforms backed by large corporations, such as Apple Music. Large drops in share price usually warrant some attention, but given our long-term mindset, we prefer to reflect on these developments in the context of a long time horizon, rather than act on impulse. As the largest service of its kind in the world, we believe Spotify can leverage its scale and significance to the broader music industry to extract better financial terms from its suppliers, continue to evolve its product, offer more exclusive content, and grow its brand profile ahead of the competition.

Spanish food retailer DIA was sold from the Fund during the quarter. We have previously been impressed by the company's management, whose strategy has been to focus on those geographic regions where the company has leading market shares (Spain, Argentina, and Brazil). Its pricing strategy, however, which resulted in relatively high and unsustainable margins, now means that its core business in Spain is facing more competition from discounters like Lidl. In the long run, there is still an opportunity to grow its business in Latin America, but we have weakening conviction in its financial returns.

Overall, there has been a shift in the Fund away from Consumer Staples companies and into Consumer Discretionary and Information Technology companies. Examples include the sale of conglomerate Nestle and food retailer Magnit, in favor of companies like Spotify and Keyence, a Japanese factory automation business. As always, we have made these decisions at the stock level, and any changes to tilts or themes are simply a byproduct of those actions.

Over the course of the year, there was relatively little change to the country allocations within the Fund. The most notable changes were an increase in active exposure to India and a decrease in active exposure to Denmark. The Danish brewing company Carlsberg was sold during the year, causing a significant reduction in relative exposure to the country. Our bottom-up approach applies here as it does anywhere else, and any over- or underweighting in a specific country should not be seen as a view on a country's market as a whole, but simply an output of the investment process.

Outlook

While the recent uncertainty in markets appears to have bred a rather pessimistic outlook among market participants, the underlying fundamentals of many companies are unchanged, as is the case for most of the Fund's holdings. The next year looks uncertain, but opportunities among international growth companies still abound, and we plan to stick to the same growth mindset we always adopt. Rather than spend excessive amounts of time trying to forecast future events, our approach remains the same as always – patient investment in a diverse portfolio of quality businesses run by sensible management.

Harbor Funds®

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ECONOMIC SECTORS

	% of Net Assets
Financials	17.52
Consumer Discretionary	16.14
Industrials	15.75
Consumer Staples	13.53
Information Technology	11.44
Communication Services	11.11
Health Care	7.43
Materials	4.91
Energy	0.85

TOP TEN HOLDINGS

Company Name	% of Net Assets
1. Naspers Ltd.	2.72
2. Hargreaves Lansdown plc	2.65
3. Taiwan Semiconductor Manufacturing Co	2.58
4. Alibaba Group Holding Ltd. ADR	2.39
5. Shiseido Co. Ltd.	2.27
6. Cochlear Ltd.	2.26
7. AIA Group Ltd.	2.07
8. United Overseas Bank Ltd.	2.05
9. MS&AD Insurance Group Holdings Inc.	2.04
10. Novozymes AS	1.96

ADDITIONAL HOLDINGS

Company Name	% of Net Assets
Asian Paints Ltd.	1.75
Auto Trader Group plc	1.67
Housing Development Finance Corp. Ltd.	1.42
Zalando Se	1.16
Spotify Technology SA	1.05
Keyence Corp.	1.04
ASOS plc	0.47
DIA	0.00
Nestle	0.00
Magnit	0.00
Carlsberg	0.00

TOTAL RETURNS

	Three Months	1 Yr.	5 Yr.	10 Yr.	Since Incp. (11/01/1993)	Expense Ratios Net	Expense Ratios Gross
Harbor International Growth Fund - *INST*	-15.17%	-16.89%	1.21%	6.56%	3.15%	0.85%	0.92%
MSCI All Country World Ex. US (ND) Index	-11.46%	-14.20%	0.68%	6.57%	N/A		

TOP TEN COUNTRIES

Country	% of Net Assets
Japan	17.71
United Kingdom	13.03
China	6.83
Germany	6.66
Sweden	6.65
India	5.79
Switzerland	5.08
Australia	4.52
South Africa	4.30
Singapore	3.91

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 an expense limitation agreement, excluding interest expense, if any, through 02/28/2019.

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. 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.

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, Baillie Gifford Overseas Limited, 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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