Harbor Core Bond Fund

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3rd Quarter, 2018 Commentary

"We believe it is important to continue to lean on our security selection skills and actively manage portfolio risk." *-Income Research + Management*

The Federal Reserve raised interest rates during the third quarter

The ongoing trade war with China, which sustained another round of tariffs in late September, has had little visible effect on the U.S. economy. The U.S. unemployment rate remained solid at 3.9%, and the Consumer Price Index increased 2.7% over the last 12 months. Gross Domestic Product growth estimates for the third quarter of 2018 hovered around 4.1%. At its September meeting, the Federal Reserve (Fed) raised interest rates, boosting the federal funds target rate to 2.00%-2.25%—the highest since October 2008. This rate hike was the third so far in 2018 and the eighth since December 2015, which started the current hiking cycle.

In this environment, the Harbor Core Bond Fund (Institutional Class) returned 0.07% during the third quarter, and outperformed its benchmark, the Bloomberg Barclays U.S. Aggregate Bond Index, which returned 0.02%. An underweight position in treasuries and an overweight position in corporate securities, namely in the Financials and Industrials sectors, contributed to relative performance. In the securitized sector, an overweight position in commercial mortgage-backed securities (MBS) and an underweight in agency MBS also benefited relative results. Detractors from relative performance included security selection Financials and Industrials, as well as in commercial MBS. Out-of-benchmark exposure to U.S. Small Business Administration securities also hindered relative results.

IR+M's comments were made in an October, 2018 report. Highlights adapted from the report appear below. All comments relate to the quarter ended September 30, 2018, unless otherwise indicated. All references to the year-to-date are for the period January 1 through September 30, 2018.

HIGHLIGHTS

Treasury Yields Increased Across the Yield Curve

Based on market-implied probabilities, there is a 70% chance that the Fed will raise interest rates in December 2018. In its most recent statement, the Fed again cited the continued strengthening of the labor market and solid economic activity. Job gains have remained robust, and unemployment has been persistently low. Treasury yields increased across the yield curve, with the 10-year yield rising 20 basis points to end the quarter at 3.06%, and the five-year yield reaching a post-crisis peak of 2.98% before retreating to 2.95% at the end of the quarter. The gap between two-year and 10-year treasury yields at quarter-end—at 0.24%—was close to its narrowest in more than a decade.

Predicting the Timing, Direction and Magnitude of Future Interest Rate Changes Is Difficult

We believe that predicting the timing, direction and magnitude of future interest rate changes is difficult to consistently get right. With this in mind, we do not maintain an outlook on interest rates. We remain committed to our disciplined, bottom-up approach while keeping the Fund duration-neutral relative to its benchmark and actively managing portfolio risk. Allocation shifts were made on the margin during the quarter, as we took advantage of long corporate spread widening in early July and participated in what we viewed as attractive new issues.

The U.S. Economic Outlook Remains Strong

Entering the fourth quarter, we believe the U.S. economic outlook remains strong, supported by a robust labor market that is driving consumer spending. The core inflation rate continues to hover around the Fed's 2% inflation rate target. The potential for an inverted yield curve still exists, in our view, but that may not deter the Fed from future tightening. The consensus view is that the Fed will raise rates again in December 2018 and three additional times in 2019. While the new Chinese tariffs have yet to significantly affect the U.S. economy, we believe the Fed could suspend its rate hikes if trade wars remain a concern.

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Recent Comments Point to Continued Monetary Policy Tightening

Recent comments made by the Fed, in addition to current market-implied probabilities, point to continued tightening of monetary policy. Historically, corporate spreads and treasury yields have moved in opposite directions. If rates continue to rise, we believe corporate spreads could grind tighter from their already historically tight level. Given this backdrop, we believe it is important to continue to lean on our security selection skills and actively manage portfolio risk.

Total Returns

As of 09/30/2018

	Three Months	One Year	Three Years	Five Years	Since Inception *(06/01/2018)*	Expense Ratios Net	Expense Ratios Gross
Harbor Core Bond Fund - INST	0.07%	N/A	N/A	N/A	0.05%	0.45%	0.68%
Bloomberg Barclays U.S. Aggregate Bond Index	0.02%	N/A	N/A	N/A	-0.10%		

Sectors: As of 09/30/2018, the Harbor Core Bond Fund had invested the following percentages of its assets in the sectors listed: Corporate Bonds & Notes, 34.78%; Mortgage Pass-Through, 24.60%; U.S. Government Obligations, 22.55%; Collateralized Mortgage Obligations, 7.66%; Asset-Backed Securities, 7.44%; Municipal Bonds, 1.95%;

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.

Performance figures discussed in any of the Manager Commentaries reflect that of the Institutional Class shares.

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

The Bloomberg Barclays U.S. Aggregate Bond Index is an unmanaged index of investment-grade fixed-rate debt issues with maturities of at least one year. This unmanaged index does not reflect fees and expenses and is 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.

The views expressed herein are those of the subadviser, Income Research + Management, and may not be reflective of their current opinions or future actions. These views are not necessarily those of Harbor Funds and should not be construed as such.

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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