



Harbor Mid Cap Value Fund



Josef Lakonishok, Ph.D.



Menno Vermeulen, CFA



Puneet Mansharamani, CFA



Greg Sleight



Guy Lakonishok, CFA

3rd Quarter, 2018 Commentary

"Value stocks are trading at significant discounts to their growth counterparts. Given current valuations, the Fund is well positioned, if and when the value style returns to favor." -LSV Asset Management

Stocks continue to rally, but value lags growth

U.S. equity markets rallied in the third quarter of 2018, bolstered by record corporate earnings, continued economic growth and progress on trade negotiations. Second quarter corporate earnings increased 27% year-over-year, while second quarter Gross Domestic Product (GDP) growth recorded a 4.2% annual gain. Unemployment remained at historic lows, and consumer and business spending increased in the quarter. The S&P 500 Index advanced 7.71%, its best quarterly gain in four-plus years. Large cap stocks outpaced mid cap and small cap equities, and value stocks continued to lag across all market cap segments.

During the third quarter of 2018, the Harbor Mid Cap Value Fund advanced 1.08%, underperforming the Fund's benchmark, the Russell Midcap® Value Index, which advanced 3.30%. Stock selection drove relative underperformance, and sector allocation also detracted. Stock choices in Information Technology were the largest drivers of relative underperformance, though favorable above-benchmark exposure to the sector lessened its negative impact. The Fund's sector weightings are purely a residual outcome of the bottom-up stock selection process.

Stock selection and an overweight in Consumer Discretionary weighed substantially on relative results, along with stock selection and an underweight in Industrials. Health Care also hindered relative performance, due to both stock choices and an unfavorable underweight. Conversely, stock selection in Financials benefited relative results substantially.

LSV Asset Management'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

A Difficult 2018 for Mid Cap Value Stocks

Mid cap value stocks continued to struggle, ending the period trailing mid cap growth stocks by more than 4%, and more than 10% year-to-date, as measured by various Russell indexes. This had a negative impact on the Fund, given our deep value bias. Many of our highest ranked companies have been punished over the past six months, despite the fact that, in our view, their fundamentals, forward earnings and cash flow estimates remain intact. For example, stock choices in the Information Technology sector dragged on returns during the third quarter. Within the sector, we find semiconductor equipment and semiconductor stocks to be attractive. However, just as they did in the second quarter, the Fund's holdings in the semiconductor equipment industry struggled, as concerns about a down cycle in the chip industry had a negative impact. Based on our valuation indicators, these companies remain attractive as long-term investments.

Following Our Formula to Find Value

We rely heavily on cash flow and earnings indicators in evaluating a stock, and we initiated a position in Allison Transmission, which ranked highly by both measures, during the quarter. The company, which designs and manufactures transmissions for commercial and defense vehicles, does not necessarily appear cheap by book value, and does not pay a notably large dividend. However, its earnings and cash flow are attractive to us, and its price momentum appears very strong, with improving margins and strong growth in both sales and earnings. The company is also aggressively buying back shares, which we see as a very positive indicator.



Harbor Mid Cap Value Fund

Consumer Discretionary and Financials at the Forefront

We do not position the Fund based on macroeconomic factors, but seek individual stocks that are undervalued. That said, throughout the year, we have increased the Fund's overweight to Consumer Discretionary. We have found attractive stocks across the sector, including auto parts, department stores, apparel retail and automotive retail companies. The Fund's overweight to Financials has also increased since the beginning of the year, primarily because the benchmark was rebalanced. The Fund is now near its maximum overweight to Financials.

Well Positioned for the Long-Term

It has been a difficult 2018 for value investors. The companies we hold in the Fund have generated strong cash flow and earnings, and in general, there has been no deterioration in their fundamentals. Yet, many have struggled in this environment. While it is difficult to time growth and value cycles, value stocks are trading at significant discounts to their growth counterparts. Given current valuations, we believe the Fund is well positioned, if and when the value style returns to favor.

Total Returns

As of 09/30/2018

	Three Months	One Year	Three Years	Five Years	Ten Years	Expense Ratios Net	Expense Ratios Gross
Harbor Mid Cap Value Fund - INST	1.08%	5.26%	10.71%	9.87%	11.67%	0.84%	0.87%
Russell Midcap® Value Index	3.30%	8.81%	13.09%	10.72%	11.29%		

Sectors: As of 09/30/2018, the Harbor Mid Cap Value Fund had invested the following percentages of its assets in the sectors listed: Financials, 22.91%; Consumer Discretionary, 15.17%; Information Technology, 11.41%; Industrials, 11.20%; Real Estate, 10.54%; Materials, 6.49%; Utilities, 6.38%; Energy, 5.37%; Consumer Staples, 4.98%; Health Care, 4.26%;

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. As of 09/30/2018, the Harbor Mid Cap Value Fund held the following position referenced as a percentage of the Fund's total net assets: Allison Transmission Holdings Inc. - 0.48%

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 02/28/2019.

The Russell Midcap® Value Index is an unmanaged index generally representative of the U.S. market for medium capitalization value stocks. This unmanaged index does not reflect fees and expenses and is not available for direct investment. The Russell Midcap® Value Index and Russell® are trademarks of Frank Russell Company.

Stocks of 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.

The views expressed herein are those of the subadviser, LSV Asset 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.

Harbor Funds is distributed by Harbor Funds Distributors, Inc.

HARBOR FUNDS and the Lighthouse Design are Reg. U.S. Pat. & Tm. Off.