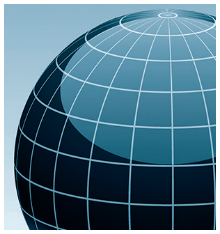
ACTIVE FIXED INCOME QUARTERLY UPDATE

Core/Core Plus Investment Strategy



December 31, 2016

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SUMMARY:

- The Republican election sweep has changed the landscape for fixed income investors.
- Following the election, we positioned portfolios neutral-to-short duration and added Treasury Inflation Protected Securities (TIPS) and corporate bonds, all of which provided a positive contribution to performance.
- Portfolios outperformed their Barclays Aggregate benchmark in the quarter.

ECONOMIC AND MARKET BACKDROP

The populist political wave around the globe in the last few years spread to the U.S. in the fourth quarter as Donald Trump defeated Hillary Clinton in the U.S. presidential election. Important for future legislation, Republicans also retained control of the Senate and the House of Representatives. President-elect Trump has stated he'll focus on reducing taxes, decreasing regulation, and increasing U.S. infrastructure investment. With the Republicans in control, we believe the legislative logjam that has existed under President Barack Obama's administration will be broken and some of these plans will be passed. Financial markets were volatile in November and December as investors grappled with the implications from the unexpected election outcome.

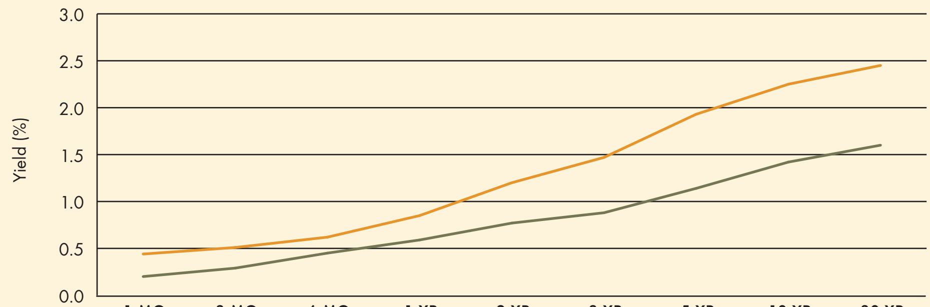
We believe the Republican sweep changed the landscape for investors. In our view, the economy and financial markets were suffering from monetary policy exhaustion, with increasing questions over the detrimental effects of low interest rates on consumers, businesses, and the financial system. The election results increase the probability that economic growth and inflation will accelerate.

The Federal Reserve has been watching these developments closely. They have wanted to raise interest rates for the past two years but have been waiting for investors to get on board. The election appears to have done this, providing the Fed with a green light to increase their benchmark federal funds rate 25 basis points in their December meeting.

DURATION/CURVE

U.S. Treasury yields increased during the quarter, led by a repricing in longer maturities of the interest rate curve. The repricing began as economists' cries that low interest rates were part of the reason consumers and businesses weren't spending reached the ears of central bankers across the globe. The unexpected outcome in the U.S. election accelerated the rise. Rates increased 79, 83, and 85 basis points across 5-, 10-, and 30-year Treasury maturities, respectively, in the steepest rise in interest rates since the Taper Tantrum in the summer 2013.

EXHIBIT 1: QUARTERLY CHANGE IN US TREASURY YIELDS



	1 MO	3 MO	6 MO	1 YR	2 YR	3 YR	5 YR	10 YR	30 YR
9/30/16	0.20	0.29	0.45	0.59	0.77	0.88	1.14	1.42	1.60
12/30/16	0.44	0.51	0.62	0.85	1.20	1.47	1.93	2.25	2.45
Change	0.24	0.22	0.17	0.26	0.43	0.59	0.79	0.83	0.85

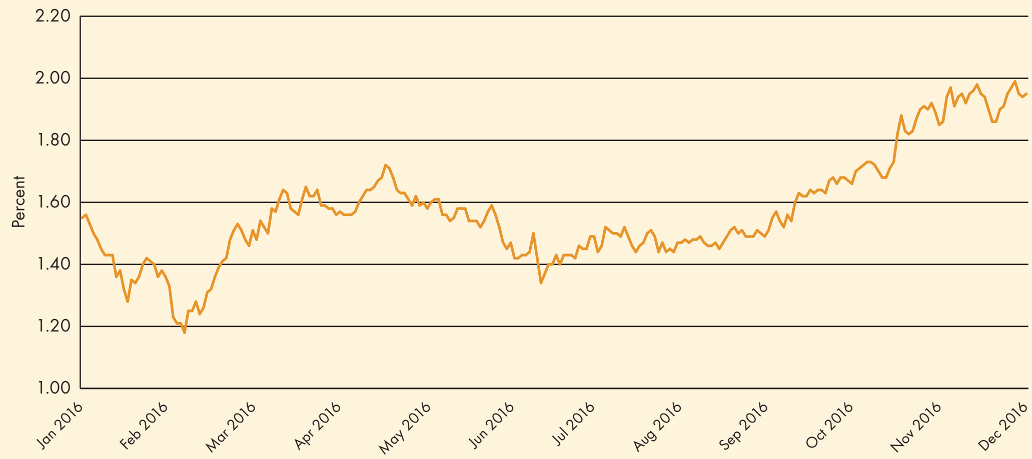
Source: Northern Trust Fixed Income; U.S. Department of the Treasury

Since the election, we changed our views on interest rates and duration positioning in our portfolios. For the last seven years we believed the U.S. economy would remain on a slow growth path and interest rates would stay low for an extended period. As such, we positioned portfolios with neutral-to-long duration versus benchmarks. However, with the likelihood of new government policies that will result in rising rates, we repositioned portfolios for neutral-to-short duration. This repositioning contributed to performance during the quarter. We believe 10-year Treasury yields will rise near-term as investors focus on the potential for more growth and higher inflation.

Inflation expectations rose in the fourth quarter from subdued levels, as evidenced by the 39 basis point increase in 10-year TIPS break-evens. Some of the inflation expectations can be tied to rising oil prices on the back of the Organization of Petroleum Exporting Countries (OPEC) agreement to reduce production. Some of the rise is also due to investors believing in an improved growth outlook for the U.S. economy.

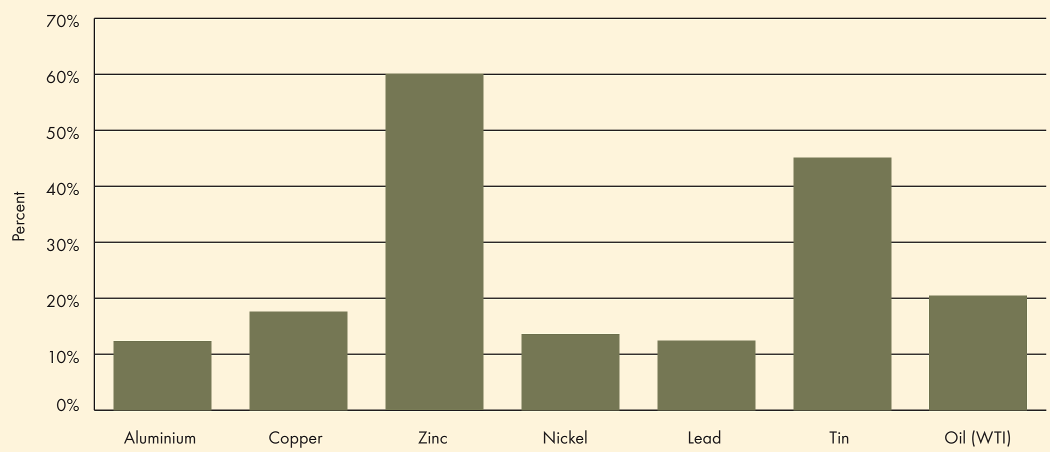
From a historical perspective, the current U.S. economic expansion is one of the longest in the post-World War II period. The economy is consistently adding jobs, unemployment is low, and there is potential for additional fiscal stimulus in 2017. We think the combination of these factors could lead to higher inflation. Accordingly, we purchased TIPS following the election. These were a positive contributor to performance in portfolios and we retained these positions entering 2017.

EXHIBIT 2: TIPS 10-YEAR BREAKEVEN INFLATION RATE



Source: Northern Trust Fixed Income; Federal Reserve Bank of St. Louis

EXHIBIT 3: 1 YEAR CHANGE IN COMMODITY PRICES AT 12/30/16

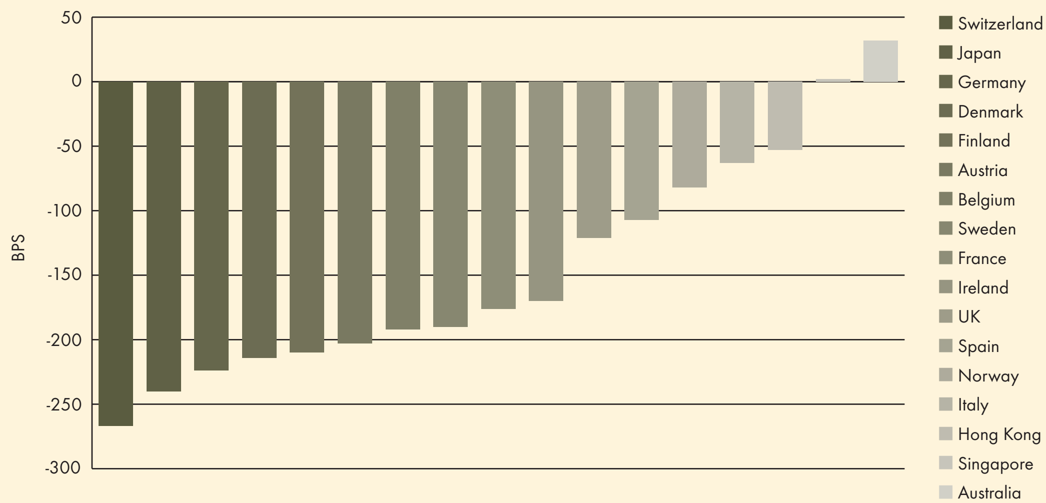


Source: Northern Trust Fixed Income; Bloomberg

SECTOR ALLOCATION

Interest rates rose across developed markets in the fourth quarter, but the U.S. continued to enjoy some of the highest rates in the developed world.

EXHIBIT 4: DEVELOPED MARKETS SPREAD TO TEN YEAR U.S. TREASURIES

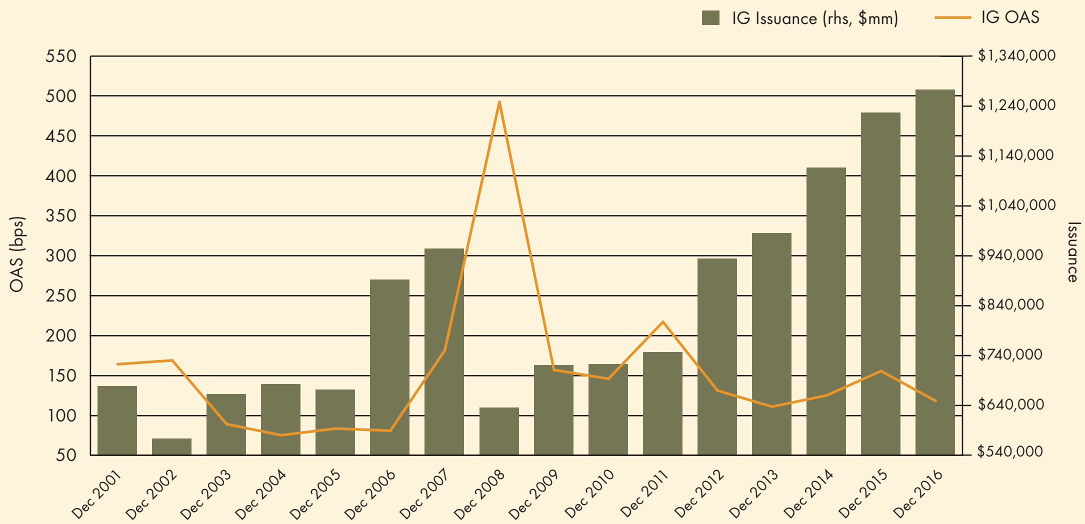


Source: Northern Trust Fixed Income; Bloomberg

The large yield advantage has led foreign investors to continue to pour money into Treasuries and U.S. investment grade corporate bonds. The new money has provided fixed income investment managers with ample ammunition to purchase bonds in the new issuance and secondary markets.

Credit spreads contracted during the quarter even though issuers continued to flood the market. Indeed, while 2016 marked the fourth record year in a row for new issuance of investment grade corporate bonds, credit spreads still tightened 37 basis points. In 2016 investment grade credit returned approximately 5.6% based on the Barclay's U.S. Credit Index as credit spreads have contracted and yields increased modestly.

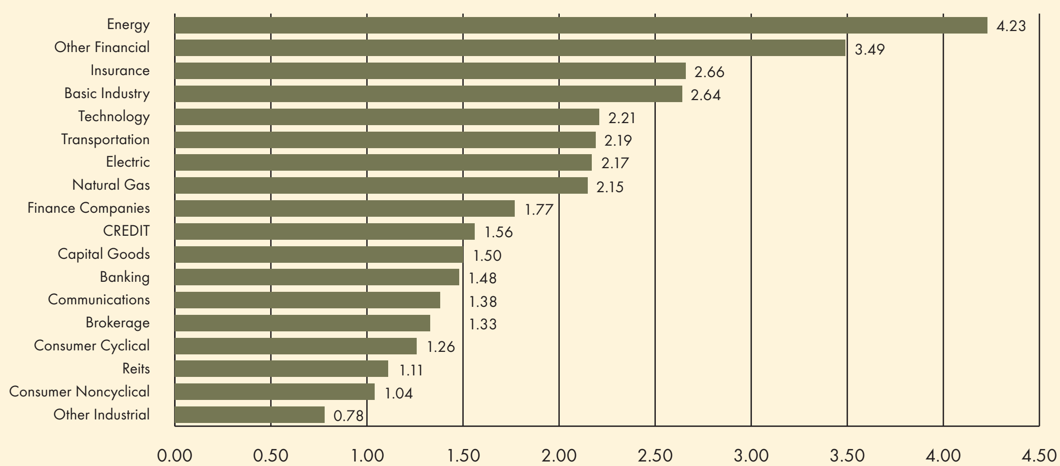
EXHIBIT 5: INVESTMENT GRADE CREDIT: ANNUAL ISSUANCE



Source: Northern Trust Fixed Income; Bloomberg Barclay's

The top performing sectors during the quarter were energy and other financials.

EXHIBIT 6: EXCESS RETURNS BY SECTOR – PAST 3 MONTHS



Source: Northern Trust Fixed Income; Bloomberg Barclay's

We moved to further overweight credit risk assets such as investment grade and high yield corporate bonds, reducing exposure to asset-backed, commercial mortgage-backed, and residential mortgage-backed debt. The decision to take more risk was a positive contributor to performance as credit spreads for corporate bonds contracted, ending the year near their tightest levels in the last two years.

Looking forward, the portfolio management team prefers corporate bonds as a way to improve total returns. We believe a key investment implication from the U.S. election is the probability of better economic growth in the U.S. has increased. This growth will be translated into increased revenue and cash flows of U.S. companies that will enhance their creditworthiness. Credit fundamentals have deteriorated due to shareholder friendly activities and record merger and acquisition activity over the past few years. We believe this trend will begin to reverse in 2017. Better economic growth, higher interest rates, and better corporate cash flows are all factors that could lead to tighter credit spreads for corporate bonds in the new year.

SECURITY SELECTION

Within our increased exposure to corporate bonds, we are overweight to the financial sector. While financial companies underperformed other sectors of the corporate bond market in 2016, we believe this will change. Higher interest rates, lower corporate tax rates, and less regulation are all potential positives for this sector. The underperformance in 2016 has created a relative value opportunity, in our opinion. In addition, financial companies are often some of the largest and most liquid issuers in the investment grade universe, which are key considerations in constructing high quality, liquid investment portfolios.

The team continues to be underweight traditional retail companies. We believe the retail business model is changing. Traditional bricks and mortar retailers are facing challenges from online competition and we expect this trend to continue in 2017.

EXHIBIT 7: PERFORMANCE AS OF DECEMBER 31, 2016

Northern Funds	1-Year Return	3-Year Avg. Annual Return	5-Year Avg. Annual Return	10-Year Avg. Annual Return	Avg. Annual Since Inception	Gross Expense Ratio	Net Expense Ratio	Inception Date
Northern Core Bond Fund[1]	2.25%	2.84%	2.59%	4.54%	4.59%	0.47%	0.43%	3/29/01
Benchmark: Bloomberg Barclays U.S. Aggregate Bond Index	2.65%	3.03%	2.23%	4.34%	4.70%	–	–	–
Northern Fixed Income Fund[1]	3.22%	3.05%	2.93%	4.28%	5.14%	0.49%	0.47%	4/1/94
Benchmark: Bloomberg Barclays U.S. Aggregate Bond Index	2.65%	3.03%	2.23%	4.34%	5.58%	–	–	–
Northern Short Bond Fund	1.81%	0.86%	1.23%	2.56%	4.02%	0.43%	0.41%	1/11/93
Benchmark: Bloomberg Barclays 1–3 Year U.S. Government/Credit Index	1.28%	0.90%	0.92%	2.44%	4.00%	–	–	–
Northern Short-Intermediate U.S. Government Bond Fund[1,2]	0.44%	0.75%	0.45%	2.21%	3.04%	0.49%	0.43%	10/1/99
Benchmark: Bloomberg Barclays 1–5 Year U.S. Government Index	1.02%	1.04%	0.80%	2.76%	3.60%	–	–	–
Northern U.S. Government Fund[1,2]	0.57%	1.31%	0.65%	2.91%	4.10%	0.83%	0.46%	4/1/94
Benchmark: Bloomberg Barclays Intermediate U.S. Government Index	1.05%	1.58%	1.04%	3.42%	4.70%	–	–	–

Performance quoted represents past performance and does not guarantee future results. Investment return and principal value will fluctuate so that shares, when redeemed, may be worth more or less than their original cost. Current performance may be lower or higher than that shown here. Performance data current to the most recent month end is available by calling 800-595-9111.

The Advisor has agreed to reimburse certain expenses of the Fund. The contractual reimbursement arrangement is expected to continue until at least July 31, 2017. After this date, the contractual arrangements may be terminated if it is determined to be in the best interest of the Fund and its shareholders. In the absence of fee waivers, yield, total return, growth since inception and dividends would have been reduced. Total return is based on net change in NAV assuming reinvestment of distributions.

Annualized for periods greater than one year.

[1]**Mortgage-Backed Securities Risk:** Mortgage-backed investments involve risk of loss due to prepayments and, like any bond, due to default. Because of the sensitivity of mortgage-related securities to changes in interest rates, the Fund's performance may be more volatile than if it did not hold these securities.

[2]**U.S. Government Guarantee:** U.S. government guarantees apply only to the underlying securities of a Fund's portfolio and not the Fund's shares.

Alpha: Measures a fund's risk-adjusted performance and represents the difference between a fund's actual performance and its expected performance, given its level of risk.

Barclays 1 – 3 Year U.S. Government/Credit Index is an unmanaged index of securities issued by the U.S. government and corporate bonds with maturities of one to three years. It is not possible to invest directly in an index.

Barclays 1 – 5 Year U.S. Government Index is an unmanaged index of securities issued by the U.S. government with maturities of one to five years. It is not possible to invest directly in an index.

Barclays Intermediate U.S. Government Index is an unmanaged index including all public obligations of the U.S. Treasury and all publicly issued debt of U.S. government agencies with maturities of up to 10 years. It is not possible to invest directly in an index.

Barclays U.S. Aggregate Bond Index is an unmanaged index of prices of U.S. dollar-denominated investment-grade fixed income securities with remaining maturities of one year and longer. It is not possible to invest directly in an index.

Basis Points (bps): Unit of measure used in quoting yields, changes in yields or differences between yields. One basis point is equal to 0.01%, or one one-hundredth of a percent of yield and 100 basis points equals 1%.

Beta: Beta represents the systematic risk of a portfolio and measures its sensitivity to a benchmark.

Bond Risk: Bond funds will tend to experience smaller fluctuations in value than stock funds. However, investors in any bond fund should anticipate fluctuations in price, especially for longer-term issues and in environments of rising interest rates.

ERISA: Employee Retirement Income Security Act of 1974 (ERISA) enacted rules for U.S. qualified plans to help protect the retirement assets.

Option-adjusted spread (OAS) is the difference in yield between two fixed income securities (generally between a fixed income security with credit risk and a comparable treasury bond), adjusted for differences in duration and embedded options.

Yield-to-Worst (YTW) is the lowest potential yield that can be received on a bond assuming options available to the issuer are exercised.

Please carefully read the prospectus and summary prospectus and consider the investment objectives, risks, charges and expenses of Northern Funds before investing. Call 800-595-9111 to obtain a prospectus and summary prospectus, which contains this and other information about the funds.

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