Highlighting attribution, economic and market analysis

HIGH YIELD FIXED INCOME QUARTERLY UPDATE

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SUMMARY:

- **The high yield market posted solid returns. Market volatility was low and company fundamentals continued to improve.**
- **Northern Trust's High Yield Fixed Income Fund was positioned for risk to perform well. It outperformed the Bloomberg Barclays U.S. Corporate High Yield 2% Issuer Capped Index.**
- **Progress on U.S. government policy objectives, monetary policy and commodity prices will continue to be the primary drivers of returns moving forward.**

PHILOSOPHY

Northern Trust's active high yield fixed income group manages portfolios to generate returns consistent with the high yield market. We use a total return approach to generate alpha through fundamental credit analysis, security selection and sector allocation. We do not employ equities, leverage or derivatives in portfolio construction. Our investment process is designed to preserve capital and manage risk by constructing well diversified investment portfolios that reflect our views on the economy, fiscal and monetary policy and market valuations.

Over time, the fund has generally been positioned in the mid-range of the credit quality spectrum of the market. The highest quality securities carry a material amount of interest rate risk and the lowest rated securities carry credit and market volatility risk. Over an extended period of time, management of credit and interest rate risk is critical for performance.

GLOBAL ECONOMY STRENGTHENS, AS FED PREPARES TO REDUCE ITS BALANCE SHEET

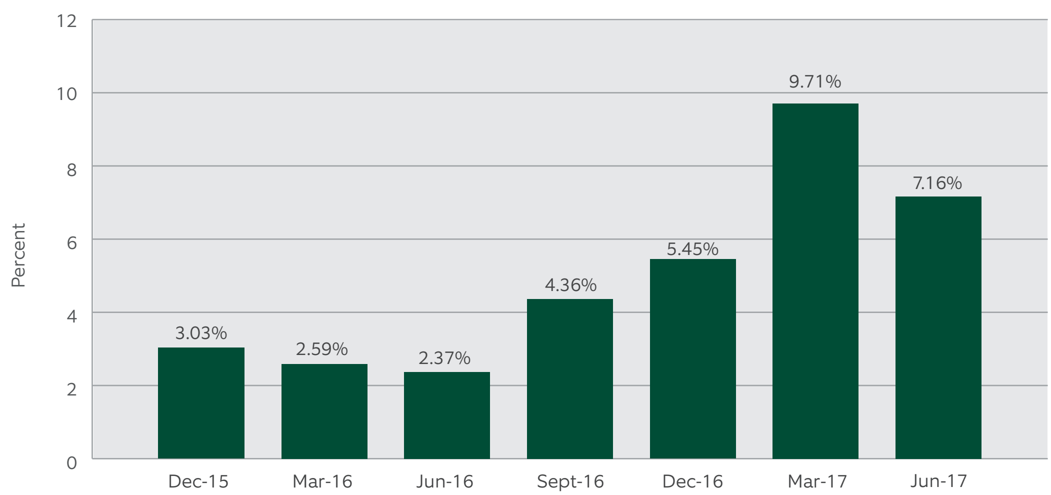
Global economic growth improved in the third quarter against a continued backdrop of low inflation. Developed economies are now all showing growth for the first time since 2010 and businesses and consumers are showing the most confidence in their prospects in a decade. Data show the U.S. expansion that began in 2009 continued, making it one of the longest since World War II. Low inflation has been a recurring theme in the global economy since the financial crisis, causing central banks to take their benchmark interest rates to all-time lows and provide additional policy accommodation through bond purchase programs.

Despite modest growth and low inflation, the Federal Reserve announced plans at their September meeting to continue slowly removing policy accommodation by reducing the size of their balance sheet. The years long plan to reduce the Treasury and mortgage-backed bonds held by the Fed started Oct. 1. The program will reduce their holdings slowly and mechanically, assuming economic conditions warrant it. With interest rates still very low historically, the Fed prefers to continue to slowly tighten policy despite recent data continuing to show the modest growth and inflation that's characterized this long expansion.

PERFORMANCE: SOLID INDEX RETURNS, LED BY OIL-RELATED SECTORS

The high yield market posted a solid return in the third quarter. Global economic growth has been better than expected in 2017, providing a positive backdrop to all risk assets. Within the high yield market, volatility was quite low. Revenue and earnings growth of high yield companies has improved debt metrics, providing support to the market.

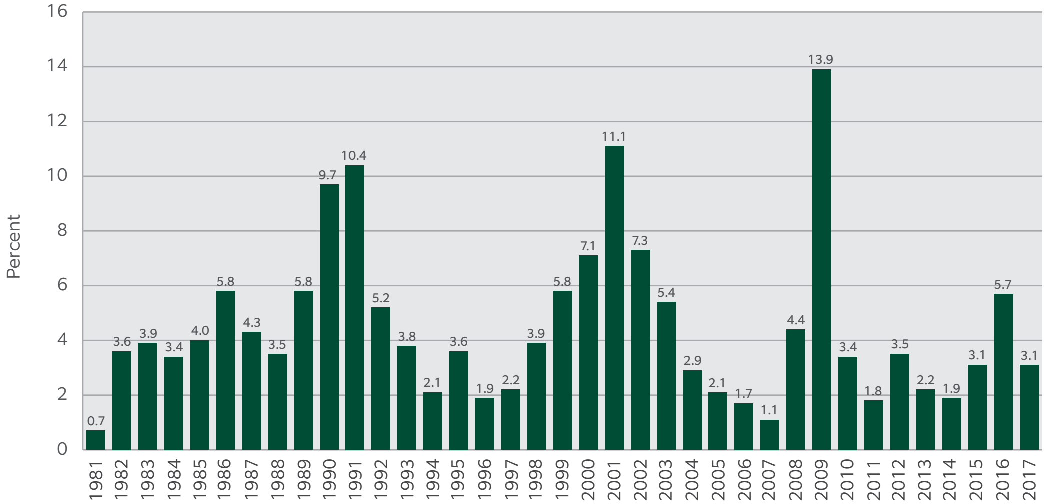
EXHIBIT 1: YEAR-OVER-YEAR REVENUE GROWTH FOR HIGH YIELD COMPANIES



SOURCE: Bloomberg Barclays Indices, Capital IQ

A 12% increase in the price of oil drove outperformance in oil-related sectors. The end of the commodity default cycle has driven defaults back to the low levels seen in much of the post-financial-crisis period.

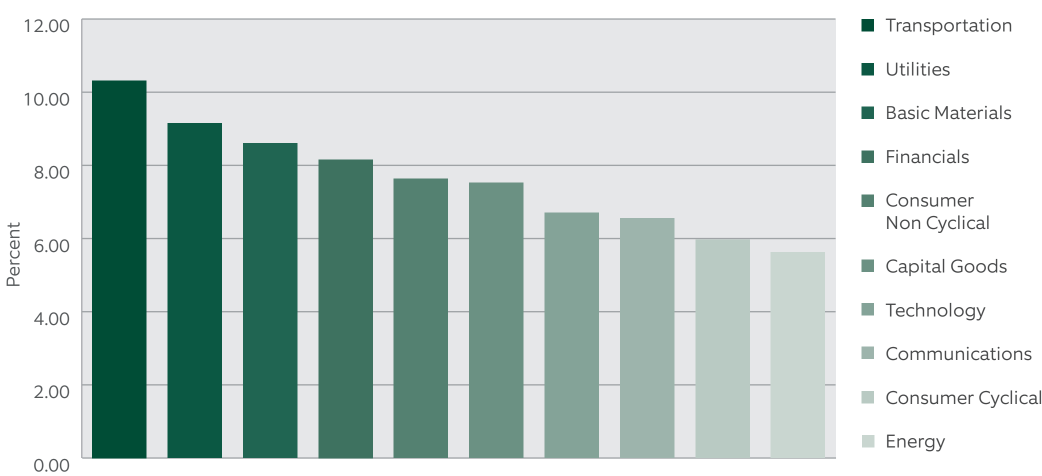
EXHIBIT 2: MOODY'S U.S. SPECULATIVE GRADE DEFAULT RATE



As of 9/30/17
SOURCE: Northern Trust Fixed Income, Bloomberg Barclays

Challenging secular trends continued to negatively affect certain sectors as the difficult retail environment spread to the supermarket and consumer product sectors. Uncertainty about U.S. health insurance policy pressured companies in the health care sector.

EXHIBIT 3: HIGH YIELD SECTOR YTD RETURNS



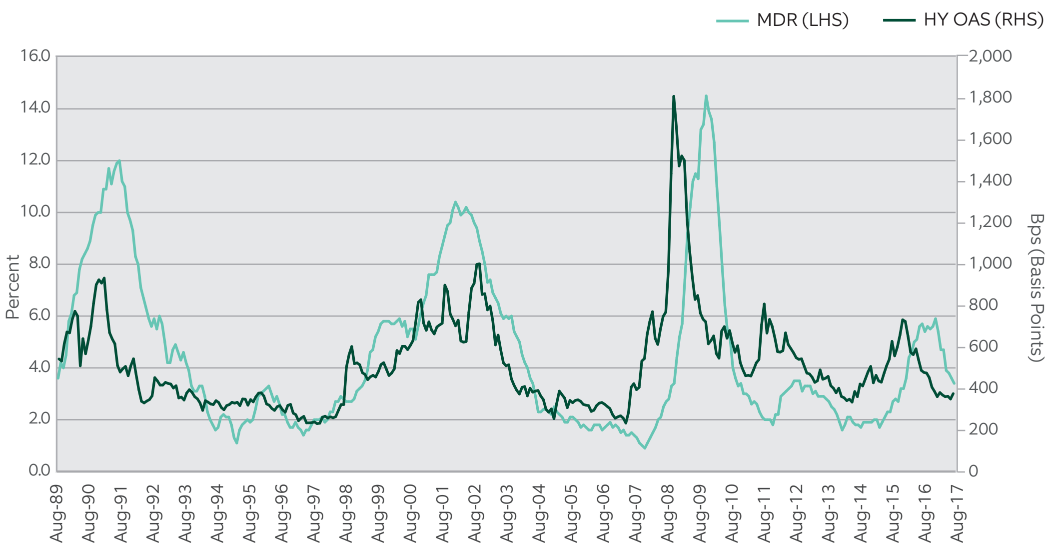
As of 9/30/17
SOURCE: Northern Trust Fixed Income, Bloomberg Barclays Live

The Fund's 2.71% return exceeded the 1.98% return of the Bloomberg Barclays U.S. Corporate High Yield 2% Issuer Capped Index. Sector selection was a more important driver of performance than credit quality. The CCC rating category performed best. This was followed by BB, B and Ca-D rated securities, in descending order. The fund was overweight CCC and B rated securities and underweight BB rated securities.

Overweight positions in refining, independent energy and metals contributed to performance. An overweight position in health care detracted from performance.

The yield to worst (YTW) on the market ended the quarter at 5.45%. Option-adjusted spreads continue to contract and are now near their tightest in the last three years. By rating, BB's closed the quarter yielding 4.04%, B's at 5.33% and CCC's at 8.47%.

EXHIBIT 4: HIGH YIELD INDEX OPTION ADJUSTED-SPREAD VERSUS MOODY'S DEFAULT RATE



SOURCE: OAS is from Bloomberg Barclays Capital 2% Capped Index, Defaults is from Moody's

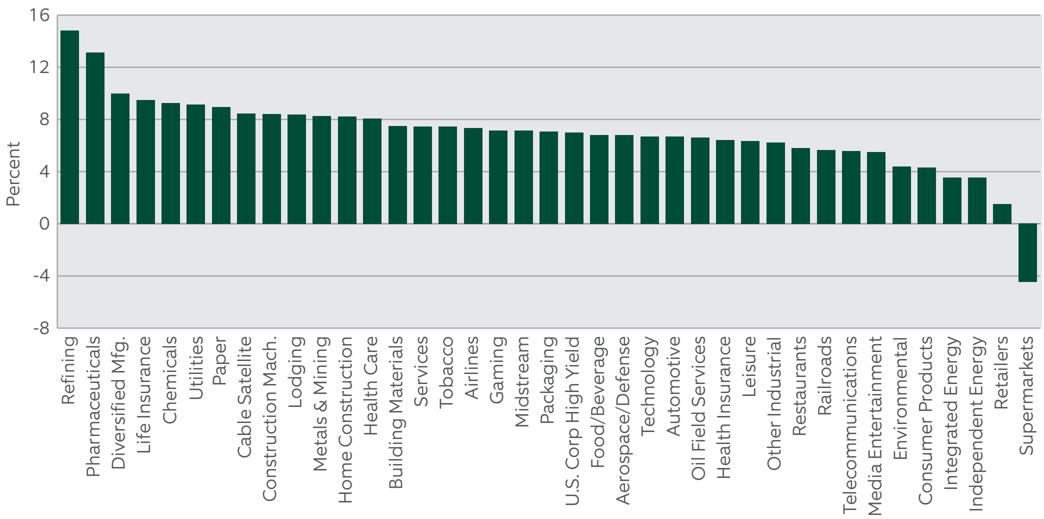
The fund maintained exposure to bank loans in select situations that offered attractive relative value. Bank loans are an asset class that's closely aligned with high yield bonds. Both represent an extension of credit to non-investment-grade borrowers. Approximately 80% of high yield issuers also have bank loans on their balance sheets. These instruments provide portfolio managers with additional flexibility, particularly when market volatility is high.

While both high yield bonds and bank loans may provide investors with the potential for more income than investment-grade bonds, we believe a few key differences make bank loans relatively safer and less volatile. As floating rate instruments priced off Libor, bank loans effectively mitigate interest rate risk that fixed rate bonds can't. They're also secured by the assets of the borrower and hold a senior position in an issuer's capital structure, creating an instrument with a lower level of credit risk. Lower interest rate and credit risk generally lead bank loans to exhibit less volatility than high yield bonds while still providing the potential for more income than investment-grade issuers.

SECTOR SPOTLIGHT: SUPERMARKETS

While the overall Bloomberg Barclays U.S. Corporate High Yield 2% Issuer Capped Index returned 7.00% through September 2017, the high yield supermarkets sub-industry returned 0.45%, making it the worst performing sector in the index. Why has this occurred and do these new prices represent an investment opportunity?

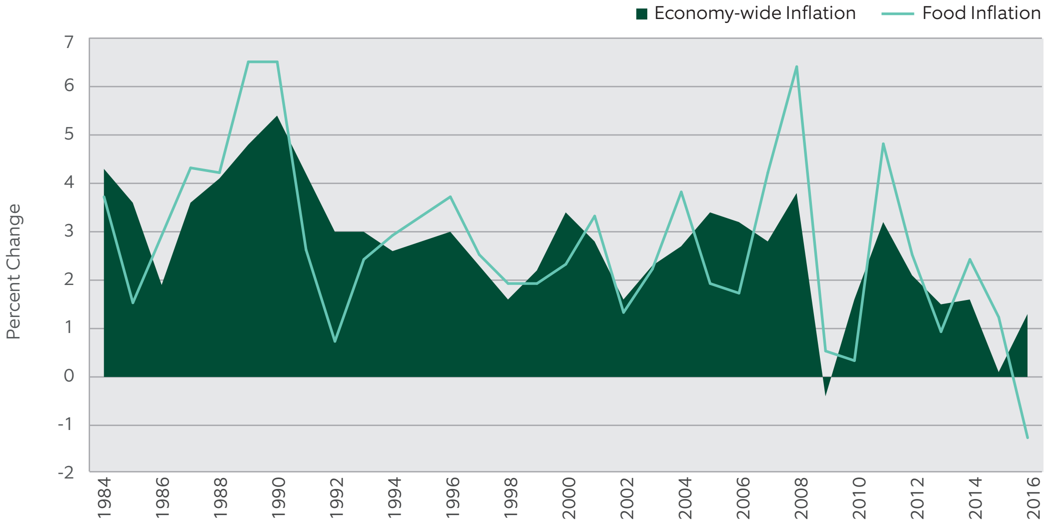
EXHIBIT 5: HIGH YIELD SUB-INDUSTRY YTD TOTAL RETURN



As of 9/30/17
SOURCE: Northern Trust Fixed Income; Bloomberg Barclays

Food price deflation and increased competition have created a challenging environment for supermarkets. Abundant crops have driven down prices of nuts, fruits, vegetables and prices of ingredients in packaged goods. Companies have passed through much of this deflation to consumers, creating an extreme promotional environment and depressing sales and profit margins. In addition, competition has been increasing in natural and organic offerings. All this makes the future look difficult for supermarkets, especially highly leveraged supermarkets that issue high yield debt.

EXHIBIT 6: PERCENT CHANGE IN THE ALL-ITEMS CONSUMER PRICE INDEX (CPI) AND FOOD CPI, 1984-2016



SOURCE: USDA, Economic Research Service, using data from the U.S. Bureau of Labor Statistics' Consumer Price Index

EXHIBIT 7: HIGH YIELD SUPERMARKETS INDEX COMPONENTS

SUPERMARKET OPERATORS	% OF INDEX
Albertsons Cos LLC / Safeway	55%
Tesco PLC	9%
The Fresh Market	9%
Ingles Markets Inc.	8%
Tops Holdings/Markets	6%
BI-LO LLC / BI-LO Finance Corp	5%

SUPERMARKET STORE SUPPLIERS	
C&S Group Enterprises LLC	4%
Supervalu Inc	4%
Kehe Distributors LLC	2%

As of 9/30/17
Source: Northern Fixed Income, Bloomberg Barclays

Amazon.com, Inc. recognizing the pressures on supermarkets and the increasingly competitive landscape for organic and natural foods, recently agreed to purchase Whole Foods Market Inc. Amazon's history of operating with low to break-even margins to build their businesses for the long term sent shivers through traditional and nontraditional food retailers, causing already stressed valuation multiples to fall further.

Investor calls hosted by Amazon, ahead of raising $16 billion to partially fund the Whole Foods Market acquisition, emphasized being able to offer Whole Foods Market's 365 private label brand on their Amazon Fresh platform. Private label products are exclusive retailer brands that cost consumers less and provide retailers with better margins than branded products. We think they could use Whole Food Market's 465 stores to get closer to customers and capitalize on the throughput of fresh products to offer a wider assortment of products that other retailers can't justify stocking. In light of the Amazon acquisition, we think it may be harder for stores to pass through food inflation in the future, keeping a ceiling on profits and valuation multiples.

SUPERMARKET OUTLOOK

While supermarket bond prices have fallen, we don't think it's time to buy issuers in this sector. We believe heightened competition will continue in the near term, limiting retailers' ability to raise prices even if food costs start to rise. We think some firms' deleveraging plans will stall due to the increasingly competitive landscape. As a result, we expect our portfolios will remain underweight high yield supermarkets.

TABLE 1: PERFORMANCE AS OF SEPTEMBER 30, 2017

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 High Yield Fixed Income[1, 2]	8.99%	4.20%	5.40%	6.13%	6.00%	0.81%	0.81%	12/31/98
Benchmark: Bloomberg Barclays U.S. Corporate High Yield 2% Issuer Capped Index	8.87%	5.84%	6.37%	7.92%	7.17%	–	–	–

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, 2018. 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]**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.

[2]**High-Yield Risk:** Although a high-yield fund's yield may be higher than that of fixed-income funds that purchase higher-rated securities, the potentially higher yield is a function of the greater risk that a high-yield fund's share price will decline.

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.

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%.

Barclays U.S. Corporate High Yield 2% Issuer Capped Index is an unmanaged index that measures the market of U.S. dollar-denominated, non-investment-grade, fixed-rate, taxable corporate bonds. It is a version of the Barclays High Yield Corporate Bond Index except it limits its exposure of each issuer to 2% of the total market value and redistributes any excess market value Index-wide on a pro-rata basis.

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.

References to specific securities within the utilities sector were made in an effort to highlight relevant news in the high yield sector during the period. For a full list of holdings for Northern High Yield Fixed Income Fund, please visits northernfunds.com. Holdings are subject to change and current and future portfolio holdings are subject to risk.

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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