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Northern Small Cap Value NOSGX

Morningstar's Take | 12-22-11 | by David Falkof

This fund's high-quality bias has benefited investors.

Northern Small Cap Value is a strong contender. Manager Bob Bergson takes a more cautious approach than the typical small-value fund. For one, he minimizes the impact of any single holding by spreading the fund's assets across 400 to 600 stocks. (By comparison, the category norm is roughly 100 holdings.) Bergson also avoids making big sector bets by keeping weightings tightly in line with the fund's benchmark, the Russell 2000 Value Index.

The fund's stock-selection process is prudent as well. Bergson uses quantitative models to screen for companies trading at low valuations relative to industry peers. The models pick businesses with steady free cash flow, high profitability, and low debt. Importantly, the process attempts to weed out the most distressed stocks and instead give the fund a high-quality tilt.

Bergson will occasionally make minor tweaks to the models in response to market opportunities. Amid 2008's financial crisis, for instance, some stocks that didn't meet the fund's quality criteria traded at cheap enough prices for Bergson to buy them on valuation alone. While those moves marginally improved returns during 2009's speculative-fueled rally, it still performed as expected; the fund held up better than 93% of its peers in 2008, but still trailed nearly all its peers in 2009.

As macroeconomic concerns have roiled the market in 2011, the fund's higher-quality stocks have held up well. Through Dec. 20, the fund's 1.4% year-to-date loss bests 80% of its peers.

Over the long haul, the fund has solidly beaten its benchmark while staying modestly ahead of its competitors. The fund has topped its benchmark in 85% of the rolling five-year periods since Bergson took the helm in July 2001. It's outpaced the category average 58% of the time. The fund's seasoned manager, disciplined strategy, and reasonably cheap fees make it a fine choice.

Strategy

The fund's manager uses a quantitative model that selects small-cap stocks that trade cheaply relative to book value. His secondary screen considers price/earnings, cash flow, and sales. The fund holds tiny positions in hundreds of stocks. Its sector weightings are now loosely aligned with the Russell 2000 Value Index's.

Management

Bob Bergson took over from Susan French in July 2001. He arrived at Northern in 1997 after serving as a director of investment research at a real estate consulting firm. Bergson is supported on the fund by a squad of quantitative analysts and researchers.

Northern Small Cap Value NOSGX

Year	Total Return (%)	+/–Category
2011	-0.61	3.84
2010	24.61	-1.56
2009	17.77	-13.55
2008	-23.43	8.81

Data through 12-31-11

NORTHERN SMALL CAP VALUE FUND

Inception 4/1/1994

AVERAGE ANNUAL TOTAL RETURNS AS OF 12/31/11				TOTAL ANNUAL OPERATING EXPENSE RATIOS	
1-Year	5-Year	10-Year	Since Inception	Gross	Net
–0.60%	0.39%	7.99%	9.19%	1.36%	1.00%

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 December 31, 2012. 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.

Equity Risk: Equity securities (stocks) are more volatile and carry more risk than other forms of investments, including investments in high-grade fixed income securities. The net asset value per share of this Fund will fluctuate as the value of the securities in the portfolio changes.

Small Cap Risk: Small-capitalization funds typically carry additional risks since smaller companies generally have a higher risk of failure. Their stocks are subject to a greater degree of volatility, trade in lower volume and may be less liquid.

Value Risk: Value-based investments are subject to the risk that the broad market may not recognize their intrinsic value.

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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 contain this and other information about the Funds.

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50 SOUTH LASALLE STREET | P.O. BOX 75986 | CHICAGO, ILLINOIS 60675-5986 | 800-595-9111 | NORTHERNFUNDS.COM