

International Investing Demystified

We're glad you could join us for a discussion on international investing. During this podcast, we will identify seven myths associated with international investing. These myths are rooted in outdated information, common misconceptions or the "fear of the unknown." Today, it's our mission to dispel these myths, and help you redraw the boundaries of your investment portfolio. Because when you limit stock investments to the United States, you limit growth potential.

Let's begin.

The United States remains home to the world's largest stock market. But, the United States isn't the only "land of stock market opportunity." Today, more than half the world's investment opportunities are located outside the United States.

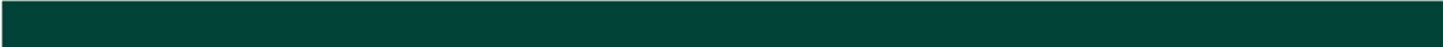
Yet, many investors remain reluctant to invest overseas. Some perceive foreign markets as unusually volatile.

For others, the thought of sending investment dollars to faraway regions is intimidating. Some investors fear the political upheaval we often read about in certain regions of the world. Others simply prefer the comfort and familiarity of the U.S. market and the U.S. dollar.

Indeed, these concerns are valid. But the reality is ... some of the best long-term investment opportunities may come from foreign stock markets.

northerntrust.com





Consider this: When you invest only in the United States, you limit your growth potential to a *single* country and a *single* economy. But, when you invest in foreign stock markets, you expand your growth opportunities—from the established and developed markets of Western Europe and Japan ... to the maturing markets of Asia and ... to the young, emerging markets of Mexico, South America and Eastern Europe.

[Myth 1]

Our first myth, “*the biggest, most successful companies are in the U.S.*,” has some elements of truth. Indeed, the United States is home to many of the world’s largest companies, and our brand of capitalism remains the model for the rest of the world.

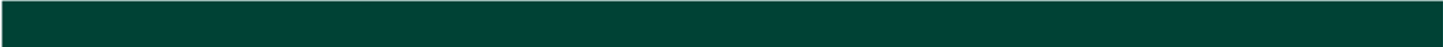
In reality, though, many of the best-known brands are headquartered overseas.

Consider the widely regarded Fortune Global 500. Nearly *two-thirds* of the companies included in the Global 500 are *non-U.S. companies*—primarily European and Asian. And 11 of the top 20 corporations on the list are foreign-based.

Also, think about your daily travels. You probably come across several companies with headquarters outside the United States. And you probably don’t even give it a second thought.

Chances are, you’ve filled your gas tank at a Shell station. Shell’s corporate headquarters is in the Netherlands.

If you have a dog, Purina dog chow may be a staple in your household. Purina’s corporate parent calls Switzerland its home. When you pay the premium on your Prudential life insurance policy, you probably don’t think about Prudential being a



British company. If your cell phone is the popular LG brand, you're using a product from a South Korean company.

The list goes on and on. So, doesn't it make sense to consider investing in the companies providing the products and services you enjoy and rely on every day, no matter where those companies are located?

Let's move on to the second myth.

[Myth 2]

Our next myth addresses the outdated fears some investors have about investing overseas. That is, "*Foreign financial reporting and accounting regulations are weak.*"

The reality is ... reporting and accounting standards are strong in many foreign countries, particularly the developed nations.

Many foreign governments have implemented regulations designed to standardize performance and accounting data. For example, the European Union requires all publicly-traded companies to use the International Financial Reporting Standards. In recent years, officials have worked together to eliminate the major differences between European and American standards.

Among the emerging markets, the quality of financial reporting can vary. Some nations have weaker accounting and financial reporting regulations than developed countries, making it difficult to assess market risk. But, many emerging-market companies have adopted U.S. GAAP, or Generally Accepted Accounting Principles.

Such companies have taken steps to enhance and improve their self-governance and public reporting, knowing investors generally insist on such information.

[Myth 3]

Our third myth relates to performance trends between the United States and the rest of the world. Many investors subscribe to the myth that ***“Performance of the world’s markets is highly correlated.”***

Skeptics of international investing point to the globalization of the world’s economies as reason to ignore international stocks. They argue the world’s markets are so intertwined, there’s really no need to invest overseas. The reality is ... at times, the difference in returns is significant.

Although it’s true the performance correlation has tightened over time, the world’s stock markets do not always move in tandem. There is still significant divergence in long-term returns, especially in comparing the performance of U.S. stocks to emerging-market stocks.

Now, let’s discuss the fourth myth.

Myth No. 4 has its roots in a confusing and often-misunderstood aspect of international investing—currency returns. Some investors erroneously believe, ***“When the U.S. economy is strong, there is no need to invest globally.”*** In reality, the currency values associated with the world’s economies can have a significant impact on returns.

One of the benefits of investing internationally is diversified currency exposure. Similar to the performance of stocks, currencies move up and down, and their exchange rate versus other currencies can change daily. The value of a company’s

stock depends on the exchange rate between the country in which the stock is domiciled and the U.S. dollar.

Historically, currency exposure has been a significant component of return. For example, approximately 2 percent of the total annualized performance of the MSCI EAFE Index, or half the cumulative return since 1969, can be attributed to currency movement.

When you invest overseas, currency fluctuations may influence your rate of return. At times, currency fluctuations may work in your favor, and at other times they may work against you.

For example, when the U.S. dollar rises against foreign currencies, you lose value, because the foreign currency is weaker and therefore translates to fewer dollars. Conversely, returns from foreign stocks, issued in foreign currencies, actually *increase* for U.S.-based investors when the U.S. dollar declines in value versus that currency. That is because when you convert foreign currency to U.S. dollars, you are able to purchase more dollars.

The bottom line: When the U.S. dollar is weak, foreign stocks may provide better returns than domestic stocks, even though the U.S. economy is strong.

Moving on to Myth No. 5 ... ***“The U.S. market consistently performs better than foreign markets.”***

As U.S.-based investors, it's easy to fall prey to this idea. We hear about U.S. stock market's performance on a daily basis. Mainstream media outlets rarely comment on foreign stock market performance, unless a particular market faces a crisis. In reality, though, foreign markets have often outperformed the U.S. market.

For example, in seven of the last 10 years the U.S. stock market, or the S&P 500 Index, posted positive annual returns. And in six of those seven years, the index generated a double-digit return. But, throughout that time period, the U.S. never was the top-performing market. Even a return of 33.4 percent in 1997 wasn't enough to earn the S&P 500 the top spot. Three other markets—those in Switzerland, Italy and Denmark—offered better performance.

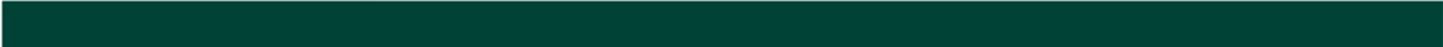
Although individual country performance demonstrates the differences in worldwide stock market returns, it may not present a realistic picture in terms of how U.S. investors behave. For example, when U.S. investors purchase foreign stocks, they typically invest in a mix of stocks from various countries, rather than one or two foreign-country stock markets.

The MSCI EAFE Index is a leading benchmark for the stock performance of developed markets outside the United States. Many international mutual funds use this index as a benchmark. Throughout the 30-year period ended December 31, 2006, the average return for the EAFE index closely matches that of the S&P 500 Index.

But, EAFE significantly outperformed the S&P 500 during various periods within that 30-year timeframe. More recently, EAFE's annual returns have exceeded those of the S&P 500 for each of the last five calendar years. EAFE's annualized return for that five-year period, 14.98%, is *more than double* the average annual return of the S&P 500.

[Myth 6]

This leads us to our next myth, “*Only developed countries offer attractive investment opportunities.*” The reality is ... emerging markets offer considerable high risk/ return investment opportunities.



Many emerging markets reside in nations with a history of political and economic instability. This means their stock prices may experience wide swings. But, in exchange for this higher degree of risk, stocks from emerging markets may offer greater long-term returns.

The emerging markets are a diverse, geographically dispersed group of 25 nations striving to strengthen and maintain economic success. They account for almost half of the world's GDP and are home to 85% of the world's population.

Unlike the developed nations of the world, many emerging-market countries are experiencing, or soon may experience, strong economic and stock market growth. In fact, Northern Trust research suggests many emerging-market countries offer double the economic growth rate of developed countries and robust company earnings.

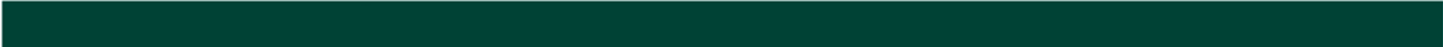
Despite occasional periods of dramatic underperformance, emerging market stocks have an 18-year history of outperforming the U.S. and non-U.S.-developed equity markets.

Nevertheless, it is important to remember the “emerging” status of these markets means they are susceptible to high volatility. As such, we recommend taking a diversified approach.

[Myth 7]

Speaking of volatility ... that's the topic of our final myth: ***“Foreign stocks add volatility to an investment portfolio.”***

This myth may be perpetuated by U.S.-based investors who avoid foreign investments in favor of the perceived “safety” and comfort of home-based holdings. In reality, *all*



investments contain some degree of volatility. And one of the most effective ways to combat volatility is to assemble a broadly diversified investment portfolio.

There are many ways to diversify a domestic stock portfolio—by company size, by investment style or by market sector or industry. But by adding international equities, you may strengthen your overall investment strategy by limiting wide swings in performance.

What's more, diversifying with overseas investments allows you to participate in the growth opportunities of various economies and markets.

Now that we've identified and dispelled several common myths tied to international investing, I hope you will consider diversifying with foreign stocks.

Remember, when you open the borders of your investment portfolio, you invite in a world of opportunity and diversification. You gain exposure to different economies, industries and stock markets, while expanding your portfolio's return potential and limiting overall volatility. Plus, international investing gives you an added level of diversification that can enhance the effects of your asset allocation strategy.

These dynamics make the global marketplace a land of investing opportunity.

Disclaimer

This commentary illustrates general principles of investing and, at times, uses the historical performance of unmanaged market indices. Index performance should not be considered indicative of the performance of any Northern Funds investment. An investment cannot be made directly in an index. Current fund performance information

may be obtained from northernfunds.com. Past performance is no guarantee of future results.

Before investing, you should carefully read the prospectus and consider the investment objectives, risks, charges and expenses of Northern Funds. A prospectus with this and other information may be obtained at 800-595-9111 or northernfunds.com.

Shares of Northern Funds are distributed by Northern Funds Distributors, LLC, not affiliated with Northern Trust. Investment advice is provided by Northern Trust Securities, Inc., a subsidiary of Northern Trust Corporation.

Not FDIC INSURED	May lose value	No bank guarantee
------------------	----------------	-------------------

2007 Northern Funds