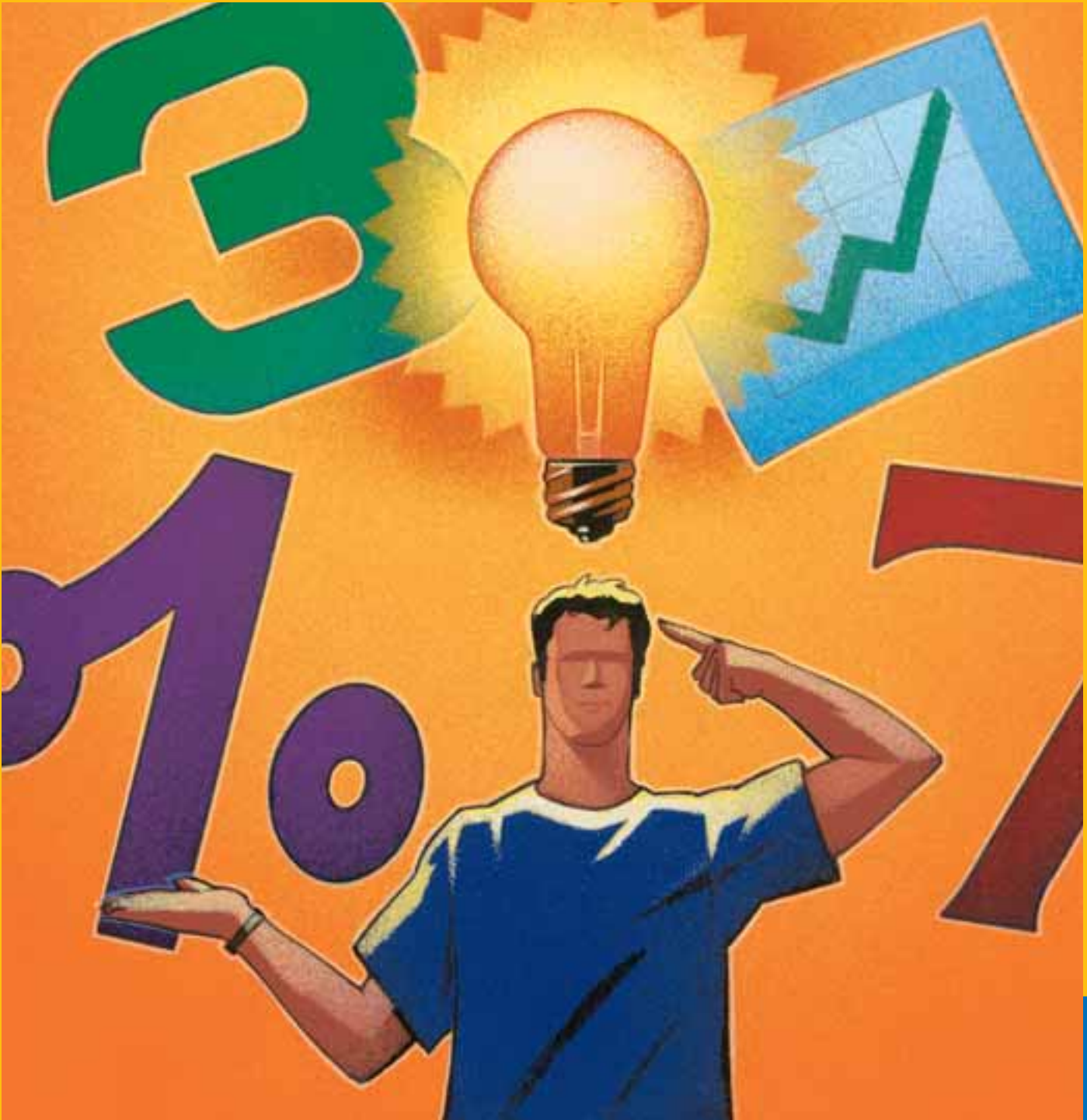


Module 6
Understanding Credit Scoring



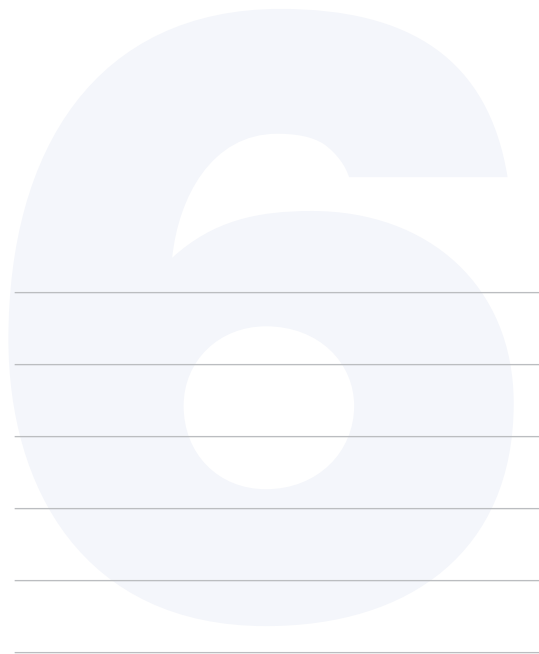
Module 6:
Understanding Credit Scoring

► **Presentation Slides**

Module

6





What Is a Credit Score?

A credit score is a computer-generated number that indicates your ability and willingness to repay a debt based on the information in your credit report.

Scores are not static; they change over time as your credit and credit behavior change over time.

Module 6-4
Understanding
Credit Scoring

What Factors Influence Credit Scores?

A credit score is based upon information drawn from an individual's credit report. There are a variety of ways that credit scoring companies determine a credit score. Based on the Fair Isaac Corporation credit scoring model, there are five primary factors (in order of importance):

1. Payment history (35%)
2. Outstanding debt (30%)
3. Credit history (15%)
4. Pursuit of new credit (10%)
5. Types of credit in use (10%)

* Source: www.myfico.com, 2007

Module 6-5
Understanding
Credit Scoring

Negative Impact on Credit Score

- Serious delinquency.
- Serious delinquency and public record or collection filed.
- Level of delinquency on accounts.
- Number of accounts with delinquency.
- Amount owed on accounts.
- Proportion of balances to credit limits on revolving accounts is too high.
- Length of time accounts have been established.
- Too many accounts with balances.

Module 6-6
Understanding
Credit Scoring



Factors Not Considered for Calculating Credit Scores

There is no inherent bias in credit scoring because only the applicant's prior credit habits are considered when calculating risk. The following factors are **not** considered when calculating a score:

- Age
- Gender
- National origin
- Sources of income
- Race
- Religion
- Marital status
- Income level

Module 6-7
Understanding
Credit Scoring

What Is the Purpose of a Credit Score?

- A credit score is a number which lenders use to help them to decide:
"If I give this person a loan or credit card, how likely is it that I will get paid back on time?"
- A credit score is used to determine whether to approve a loan and how much interest and fees to charge.

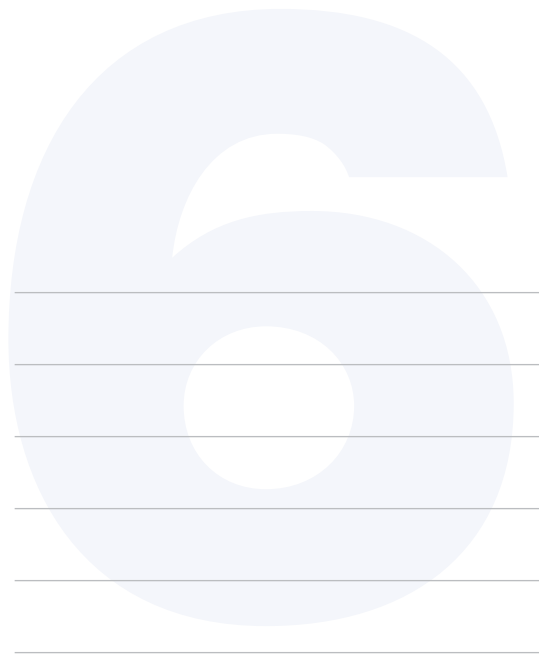
Module 6-8
Understanding
Credit Scoring

Types of Credit Scores

There are many types of credit scores; however, the most commonly used are **credit reporting agency scores**.

Credit reporting agency scores are based solely on information contained in consumer credit reports.

Module 6-9
Understanding
Credit Scoring



How Is a Credit Score Generated?

Credit scores are generated by comparing your credit report information to thousands of other credit reports.

This comparison process produces a score which identifies your level of future credit risk.

Module 6-10
Understanding
Credit Scoring

What Is Contained in a Credit Score?

Your credit score will assign a score (a numerical value) which indicates how likely you are to repay a loan.

In addition, credit scores may provide a list of the general reasons or factors which had the greatest negative impact on the calculation of your credit score.

Module 6-11
Understanding
Credit Scoring

Can I Improve My Credit Score?

Caution: It is important to note that raising your score takes time. There is no quick fix. In fact, quick-fix efforts can backfire.

Therefore, always make sure that the information in your credit report is correct and manage your credit responsibly over time.

Module 6-12
Understanding
Credit Scoring

Tips for Raising Your Credit Score



- Pay your bills on time.
- If you have missed payments, get current and stay current.
- Be aware that paying off a collection account will not *remove* it from your credit report.
- If you are having trouble paying your bills, contact your creditors or see a legitimate credit counselor.
- Keep balances low on credit cards and other revolving credit.
- Do not have too many credit cards, and do not use the maximum credit limit on any of them.

Module 6-13
Understanding
Credit Scoring

Tips for Raising Your Credit Score



- Pay off debt rather than moving it around.
- Don't close unused credit cards as a short-term strategy to raise your score.
- Don't open a number of new credit cards that you don't need just to increase your available credit.
- If you have been managing credit for a short time, don't open a lot of new accounts too rapidly.
- Do your rate shopping for a given loan within a focused period of time.

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Understanding
Credit Scoring

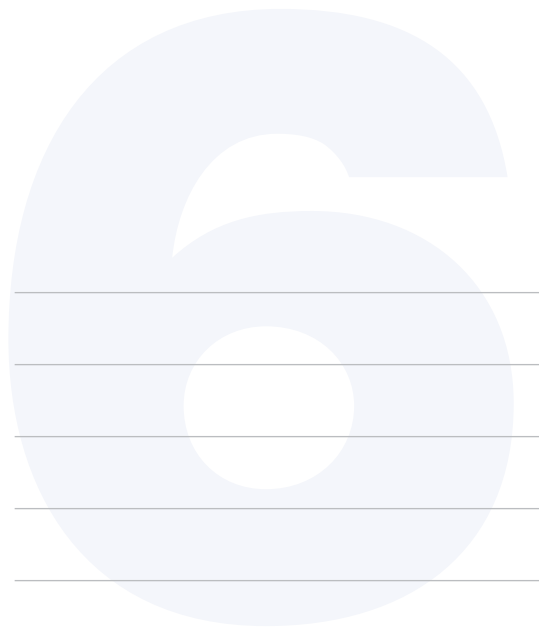


Tips for Raising Your Credit Score



- Note that it is OK to request and check your own credit report.
- Apply for and open new credit accounts only as needed.
- Have credit cards—but manage them responsibly.
- Note that closing an account doesn't make it “go away.”

Module 6-15
Understanding
Credit Scoring



What Is a Good Credit Score?

There are several types of scoring systems and each has a different scoring (rating) method. Therefore, it depends on the credit scoring model and the lender.

When applying for a loan, ask your lender or creditor to explain what your credit score means in relation to the final credit decision.

Module 6-16
Understanding
Credit Scoring

Credit Scores

Remember:

Credit scores reflect a person's long-term patterns of credit usage and repayment history.

Scores automatically improve as your overall credit picture gets better or shows a historical pattern of paying your bills on time.

Module 6-17
Understanding
Credit Scoring

Summary of Tips on Improving Your Credit Score

1. Pay your bills consistently and on time.
2. Check your credit report and correct any errors.
3. Keep credit card balances low.
4. Maintain only a reasonable amount of unused credit.
5. Do not excessively shop for unsecured credit.
6. Establish credit and use it wisely.

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Understanding
Credit Scoring

► Credit Scoring Factors and Ratings

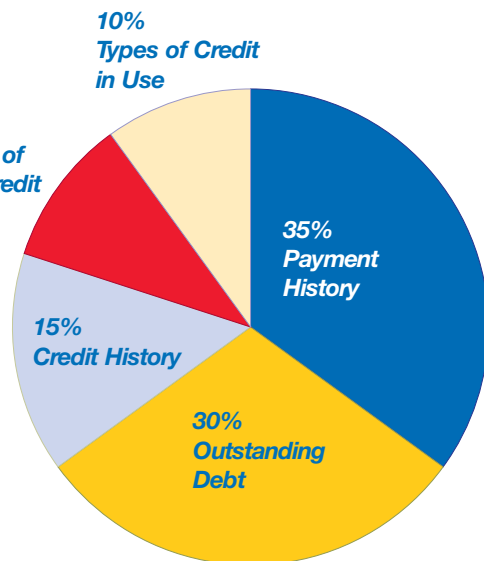
A credit score is based upon information drawn from an individual's credit report. According to Fair Isaac Corporation (FICO), about 30 individual factors are used to determine the score. These factors, known as predictive variables, can be categorized into five primary areas (in order of importance):



- 1) **Payment history**
- 2) **Outstanding debt**
- 3) **Credit history**
- 4) **Pursuit of new credit**
- 5) **Types of credit in use**

The following provides some questions relating to each of the factors and the approximate weight given to each category.

- 1) **Payment history:** What is your track record? Have your payments been made on time? **(35%)**
- 2) **Outstanding debt:** How much do you owe? Do you have a high level of debt? That is, are you near the maximum on some or all of your credit limits? **(30%)**
- 3) **Credit history:** What is the length of your credit history? That is, how long have you had credit? The longer the better. **(15%)**
- 4) **Pursuit of new credit:** Does your credit report indicate that you have made numerous applications for new credit and are potentially taking on too much debt? **(10%)**
- 5) **Types of credit in use:** Does your credit report show a "healthy" mix of credit types in use? The score will consider your mix of credit cards, retail accounts, installment loans, finance company accounts, and mortgage loans. It is important to note, however, that it is **NOT** necessary to have one of each, nor is it a good idea to open credit accounts that you do not intend to use. **(10%)**



Source: www.myfico.com, 2007. Percentages subject to change.

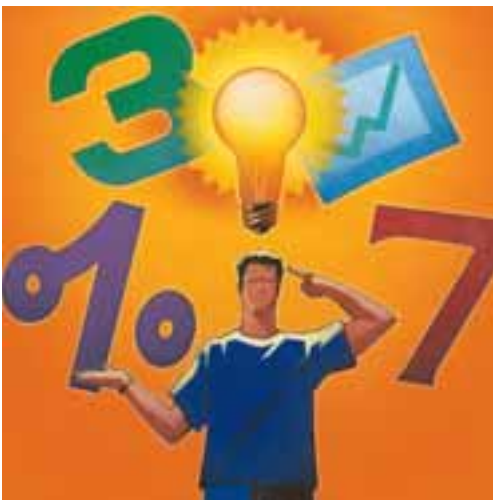
There is no inherent bias in credit scoring because only the applicant's prior credit habits are considered when calculating risk.

The following factors are NOT considered when calculating a score:

- **Age**
- **Race**
- **Gender**
- **Religion**
- **National Origin**
- **Marital Status**
- **Sources of Income**
- **Income Level**

► **Tips to Help You Maintain and Improve Your Credit Score**

- 1) Pay your bills consistently and on time.
- 2) Check your credit report and correct any errors.
- 3) Keep credit card balances low.
- 4) Maintain only a reasonable amount of new credit accounts.
- 5) Do not excessively shop for unsecured credit.
- 6) Establish credit and use it wisely.



A copy of your FICO credit score may be obtained online for a fee at www.myfico.com. This Web site also offers additional information on credit scoring, factors, and credit tips.

