Credit Scoring 101: A Beginner's Guide

A simplified introduction based on the Credit Scoring Primer

What is a Credit Score?

A credit score is a number (300-850) that predicts how likely you are to pay back borrowed money. Higher = better.

Why it matters: Lenders use your score to decide whether to approve you and what interest rate to charge. A higher score = better rates = less money paid in interest.

The 5 Things That Affect Your Score

Think of your score like a pie with 5 slices:

1. Payment History (35%) - THE BIG ONE

What it is: Whether you pay your bills on time.

Key points:

- One late payment can drop your score 50-100+ points
- The more recent the late, the worse the damage
- After 7 years, most negative items fall off

What to do: Pay at least the minimum on everything, every month, on time.

2. How Much You Owe (30%)

What it is: How much of your available credit you're using (called "utilization").

The magic number: Keep your credit card balances below **9.5%** of your limits.

Example:

- You have a card with a $1,000 limit

- Keep your balance below $95 when the statement closes
- Even better: below $45 (4.5%) for maximum points

Warning - The "All Zero" Trap:

If ALL your cards report $0 balance, you actually LOSE 10-25 points! Keep a small balance ($5-20) on ONE card.

3. How Long You've Had Credit (15%)

What it is: The age of your credit accounts.

Key points:

- Older accounts = better
- Don't close old cards, even if you don't use them
- Opening new accounts lowers your average age

Important thresholds:

- 36 months (3 years): You move to a "mature" scorecard
- 90 months (7.5 years): Believed to be near maximum benefit

4. New Credit (10%)

What it is: Recent applications for credit.

Key points:

- Each application creates a "hard inquiry"
- Inquiries hurt your score for 12 months
- They fall off your report after 24-26 months
- Multiple inquiries for the same type of loan within 14-45 days count as one

The Chase 5/24 Rule: Chase will deny most credit cards if you've opened 5+ cards (any bank) in the last 24 months.

5. Credit Mix (10%)

What it is: The variety of credit types you have.

Good to have a mix of:

- Credit cards (revolving credit)
- Auto loan, mortgage, student loans (installment loans)

Ideal ratio: About 3-4 credit cards to 1 loan.

Quick Wins to Improve Your Score

1. Pay Down Credit Cards

Get all cards below 9.5% utilization. This can boost your score in just one billing cycle.

2. AZEO Strategy (All Zero Except One)

- Pay all cards to $0 before their statement dates
- Leave a small balance ($5-50) on ONE card
- This gives you low utilization without the All-Zero penalty

3. Don't Close Old Cards

Even if you don't use a card, keeping it open helps your:

- Average age of accounts
- Total available credit (lowers utilization)

4. Become an Authorized User

Ask a family member with a long-standing, well-managed credit card to add you as an authorized user. Their good history can boost your score.

5. Stop Applying for Credit

Every application hurts your score. If you're trying to improve, stop applying for 6-12 months ("gardening").

Common Myths Debunked

■ *"Checking my own score hurts it"*

Truth: Checking your own score is a "soft inquiry" and has NO effect.

■ *"I need to carry a balance to build credit"*

Truth: You don't. Pay your full balance each month. Just make sure the statement shows a small balance before you pay it.

■ *"Closing cards I don't use will help"*

Truth: It usually hurts. It reduces your available credit and can lower your average account age.

■ *"My income affects my score"*

Truth: Income is NOT part of your credit score. Lenders consider it separately.

■ *"All credit scores are the same"*

Truth: There are many different scoring models. FICO 8 is the most common, but mortgages use FICO 2/4/5.

The Scorecards System (Advanced but Important)

FICO doesn't score everyone the same way. You're placed on one of 12 "scorecards" based on your profile:

Clean scorecards (no major negatives):

- Thick (4+ accounts) vs Thin (fewer accounts)
- Mature (oldest account 3+ years) vs Young
- No New Revolver (no new cards in 12 months) vs New Revolver

Dirty scorecards (have major negatives like 60+ day lates, collections, bankruptcy):

- You're compared against others with similar negatives
- This limits your maximum achievable score

Why this matters: When you cross a threshold (like hitting 3 years), you change scorecards. This can cause a temporary score drop even though it's actually progress!

Fixing Negative Items

For Accurate Negative Items (you really were late):

1. **Wait it out** - Impact decreases over time
2. **Goodwill letter -** Ask the creditor nicely to remove it
3. **Use the Saturation Technique** - Send letters to multiple addresses

For Inaccurate Items (errors on your report):

1. **Dispute with the bureau** (Equifax, Experian, TransUnion)
2. Provide documentation
3. They have 30 days to investigate

Your Action Plan

1. **Get your free credit reports** at AnnualCreditReport.com
2. **Check for errors** and dispute any inaccuracies
3. **Pay down cards** to below 9.5% utilization
4. **Set up autopay** for at least minimum payments
5. **Stop applying** for new credit for a while
6. **Use the toolkit** at this site to track your progress

Glossary

For the full technical details, see the complete [Credit Scoring Primer](Credit_Scoring_Primer_v2.pdf).