06/09/2007

# Three Steps to Better Credit

With all of the turmoil in the subprime mortgage market, many people with poor credit that would have qualified for a home loan a year ago are no longer being considered for mortgage funding. As more and more bad-credit homeowners file for foreclosure, lenders are taking fewer risks on those with less-than-perfect credit. If you fall into this category, and you are hoping to buy a home soon, you may need to first concentrate on improving your credit score before you will be approved.

First you need to understand what a credit score is. It is a number generally between 300 and 800 and is a composite of several different factors, including your history of on-time or late payments, the number of credit accounts you have and the balances on those accounts, and the length of time you have had credit accounts open, bankruptcies, or foreclosures, among other things. Lenders use this information to judge how likely it is that you will repay the money they loan you.

If your credit is in need of repair, try these three important steps to get back on the right path.

Step 1: Correct Errors
You should obtain a copy of your own credit report and score and scour the documents for any false information. If your report lists some payments as being later than 30 days, but you have proof to the contrary, you can challenge the error. You can do this by contacting the appropriate credit reporting agency (Experian, Equifax, or TransUnion) and providing them with the correct information. If they agree with your argument you could see some improvement to your credit score within the next month or two.

Step 2: Reduce High Credit Balances
If you have large balances on your credit cards, paying them off or significantly reducing them can really improve your credit score. If your balance is at or very close to your credit limit, the credit bureaus will perceive this as evidence of poor credit management on your part. If you can afford to do so, pay off one of those high balances. Some experts estimate that doing so could raise your score by 60-70 points in a matter of days. Similarly, if you do need to make large purchases on credit, be sure to spread out your charges on different credit cards. It is best if you can avoid spending more than 50 percent of your credit limit on any one card.

Step 3: Don’t Open New Credit Accounts
If you are getting close to applying for a new home loan, the last thing you want to do is to apply for new credit lines. To the credit bureaus, this action makes it seem like you are desperate for more funding for your lifestyle and spending habits, and it will be negatively reflected on your credit score. Similarly, do not close any unused credit accounts right before or during a mortgage application, as this will decrease your debt-to-available credit ratio. Save any opening or closing of accounts, or any major new purchases until your home mortgage loan application has been approved.