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The Paradox of Plastic: How to Build Your Credit Score

by Advisor Voices (<http://www.nerdwallet.com/blog/finance/author/advisorvoices/>) on April 8, 2014 | posted in Advisor Voices (<http://www.nerdwallet.com/blog/finance/category/advisorvoices/>)

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By Tracy Becker (<http://www.nerdwallet.com/finance/financial-advisors/advisors/profile/938/tracy-becker>)

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For some people, carrying many credit cards and accounts can result in a higher credit score. For others, a lower one. How can this be? Welcome to the paradoxical world of credit scoring.

Having a variety of credit with a nice mix of credit cards, store cards, mortgage accounts, student loans and car loans/leases over long periods of time can build a strong credit portfolio and high scores. When a consumer has a well-rounded credit portfolio with aged accounts that have stayed current, it reflects great credit management skills, which add points to the consumer's credit scores. Juggling and building a lot of credit, without delinquencies, shows lenders that the credit holder is a responsible and seasoned borrower with a low risk of default.

On the other hand, if a borrower has been in the credit game for, say, six years and opened four new accounts in the past three to six months, he would be seen as a much higher risk and his scores would drop. When someone with young credit (the age of credit is determined by the date their first account was opened) has doubled their number of credit accounts within a short period, it can be cause for concern. Since this individual has limited experience managing credit and has doubled his accounts, their scores may reflect their new greater risk of default and be lower.

Let's consider two consumers and look at exactly what their credit reflects:

Consumer A is 53 years old and has been developing credit for 35 years. Her FICO credit score is an amazing 820 and she has never had a delinquency. These are the accounts on her credit report:

14 open and active credit cards, including store cards, MasterCard, Visa and American Express

- Credit card limits equal to \$120,000
- Three closed credit cards that were opened over 28 years ago
- A balance-to-limit ratio on revolving credit of 5%
- A current mortgage that was opened eight years ago
- A closed mortgage that is still showing on her credit report that was opened 26 years ago
- Three car loans/leases that are paid and closed
- One current car loan that was opened three years ago
- No third-party credit reviews in the past two years

Consumer B is a 29-year-old who has been developing credit for six years. His FICO credit score is a 620 and he has no delinquencies. The accounts on his credit report are:

- Seven open and active credit cards, including store cards, MasterCard and Visa
- Three of the cards were opened five to six years ago; four were opened in the last three to six months
- Credit card limits equal to \$10,000
- A balance-to-limit ratio on revolving credit of 20%
- One auto loan opened four years ago

If Consumer B had kept his credit accounts to only three, and not taken out the four newer cards, his score would have been anywhere from 680 to 710. When applying for a mortgage, the difference between a 620 and 680-710 could mean enormous savings on fees, insurance premiums and interest rates, or the difference between being rejected or approved depending on the loan. For this individual, going from three accounts to seven in such a short time signaled too many accounts for his credit level and dropped scores dramatically.

But for Consumer A, someone with many years of developing varied types of credit, the 16 total active accounts are not reflective of too much credit. Instead, they've led to amazing credit scores showing a low risk of default. Using a strategy for developing healthy credit scores and variety of credit, with a timeline for your goals, can make a world of difference for your success.

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