Ask the Expert: Bill Kusman, president First Bank Mortgage

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How does a home buyer's credit score affect mortgage interest rates?

In 2008, the Federal National Mortgage Association and Freddie Mac instituted a "risk based pricing matrix." The pricing matrix, which may affect the price of a mortgage loan, is constructed around three primary drivers: credit score, loan to value and loan duration.

For example, a borrower who puts down a 25 percent down payment and has a credit score of 740 or greater might qualify for an interest rate 1/8 percent lower than someone with a smaller down payment or lesser credit score. Credit scores in the low 600s combined with a down payment of 10 percent or less can mean an interest rate as much as 1.5 percent higher than borrowers with a high credit score.

Credit scores are provided to mortgage lenders by the three major credit reporting agencies: Equifax, Experian and Trans Union. Each agency's score might be somewhat different. Most lenders use the middle scores as their policy drivers. Credit scores are measured on a scale from 300 to 850. The national credit score average in the United States is 692 with 58 percent of the population having a score greater than 700. Credit scores are influenced by two primary behaviors: payment history and outstanding debt. Statistically, a credit score is simply an indicator of how likely someone is to pay creditors.

There is an alternative to "risk based pricing." In amounts up to $281,750, the Federal Housing Administration and Veteran Administration have interest rates that are not driven by credit scores or down payments. While most mortgage lenders maintain a minimum credit score requirement of 620, FHA and VA loans, in certain cases, will be made to individuals with a score greater than 580.

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