

THE CHALLENGE

Marcus needs \$1,500 for an emergency car repair to keep his job. With a credit score of 650, he's considering three options: a credit union personal loan at 8% APR, his credit card at 18% APR, or a payday loan advertising "quick cash." The payday loan seems easiest, but the fine print shows a 400% APR equivalent.

How can Marcus determine which credit source will cost him the least and keep him out of a debt trap?

Learning Objectives

- Compare different credit sources including banks, credit unions, and alternative lenders.
- Evaluate credit options based on APR, fees, terms, and total cost.
- Identify warning signs of predatory lending and develop strategies to avoid high-cost debt.

CORE CONCEPTS

Term	Definition
Credit Union	A member-owned, not-for-profit financial cooperative that often offers lower rates than banks.
Payday Lender	A lender offering small, short-term loans with extremely high interest rates (often 300-500% APR).
Creditworthiness	A measure of how likely a borrower is to repay debt, based on credit history and score.
Predatory Lending	Unfair lending practices that take advantage of borrowers through deceptive terms or excessive fees.
Origination Fee	An upfront fee charged by a lender for processing a new loan application.

Background: Not all credit sources are created equal. Banks, credit unions, online lenders, and payday lenders all serve different purposes and come with vastly different costs. A credit union might charge 8% APR on a personal loan, while a payday lender charges 400% for the same amount. Understanding these differences can save you hundreds or even thousands of dollars. The key is to **compare multiple options** before borrowing and always calculate the total cost—not just the monthly payment or how quickly you can get the money.

APPLY IT

PART A: CREDIT SOURCE MATCHING

For each borrowing scenario, identify the most appropriate credit source and explain why.

Scenario 1: First-Time Home Buyer

Jasmine has excellent credit (780) and wants to buy her first home. She's comparing offers from her bank, a credit union, and an online mortgage lender.

Best source: _____ (bank / credit union / online lender)

Because: _____

Scenario 2: Unexpected Medical Bill

Derek has fair credit (620) and just received a \$2,000 medical bill. He has no emergency fund. A payday lender offers same-day approval; his credit union needs 3 days.

Best source: _____ (payday lender / credit union / credit card)

Because: _____

Scenario 3: Starting a Small Business

Aisha wants to borrow \$15,000 to start a food truck business. She has good credit (700) but limited business history. Traditional banks have rejected her application.

Best source: _____ (SBA loan / peer-to-peer / consumer finance)

Because: _____

Hint: Consider not just the interest rate, but also approval requirements, processing time, and total cost over the loan term.

PART B: COST COMPARISON ANALYSIS

Compare the cost of borrowing \$1,500 from different sources. Complete the missing values.

Credit Source	APR	Term	Monthly Payment	Total Interest
Credit Union Loan	8%	12 months	\$130	\$60
Credit Card	18%	12 months	\$138	\$156

Payday Loan*	400%	2 weeks	\$1,730	\$230
Total Repaid				

*Payday loan assumes single 2-week term; many borrowers roll over multiple times

4. If someone rolls over a payday loan 4 times (8 weeks total), paying \$230 in fees each time, what is the total cost?

Show your work:

Total fees paid: \$_____

5. Why might someone choose a payday loan despite the much higher cost? What alternatives should they consider?

PART C: PERSONAL CREDIT STRATEGY

6. Rank these credit sources from 1 (best/first choice) to 5 (worst/last resort) for your personal use. Explain your top and bottom choices.

___ Credit Union ___ Bank ___ Credit Card ___ Online Lender ___ Payday Lender

7. What THREE warning signs would tell you a lender might be predatory?

CHECK YOUR UNDERSTANDING

1. Which type of lender typically offers the lowest interest rates to qualified borrowers?

- ☐ A. Payday lenders
- ☐ B. Consumer finance companies
- ☐ C. Credit unions
- ☐ D. Retail store credit

2. Explain why credit unions often offer better rates than commercial banks.

3. Calculation: A bank offers a \$5,000 personal loan at 10% APR for 3 years with a \$100 origination fee. Monthly payment is \$161. What is the total cost including the fee?

Show your work:

Total cost: \$_____

4. Marcus chose the credit union loan (8% APR) over the payday loan for his \$1,500 car repair. If he pays off the credit union loan in 12 months, how much does he save compared to rolling over the payday loan 4 times?

5. Reflection: Imagine a friend is about to take out a payday loan because they need money fast. What would you say to them? What alternatives would you suggest?
