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Pros and cons of an adjustable-rate mortgage (ARM)

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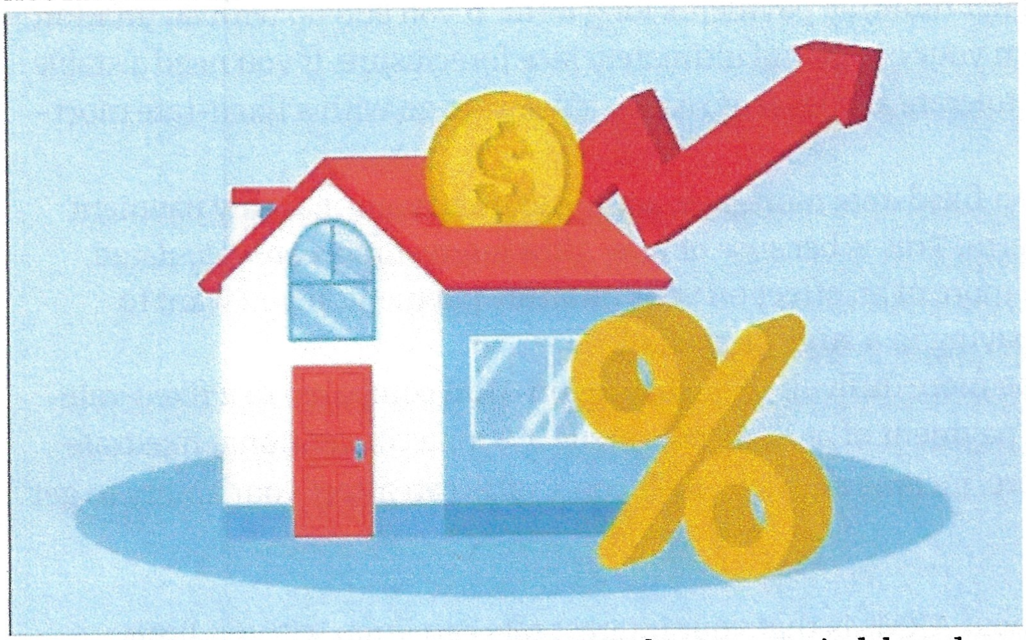
The appeal of an adjustable-rate mortgage (ARM) is simple. You often start with a lower interest rate and a lower monthly payment than you would get with a fixed-rate mortgage. But that lower rate may not last forever.



The ARM starts with a fixed interest rate for a set period, but then your rate can go up or down at set times for the rest of the loan. If you have room in your budget for potential payment changes, that lower payment could be worth it. ARMs are not the best choice for people who aren't comfortable managing uncertainty. Before deciding, make sure you not only find a loan that works for your budget today but also your plans for the future.

An adjustable-rate mortgage's main advantage is its lower initial interest rate than that of a comparable fixedrate mortgage. As of July 28, 2026, the average rate on a 5/1 ARM was 6.13%, compared with 6.60% for a 30year fixed-rate mortgage, according to Bankrate's national survey of lenders.

If you're planning to sell your home before the fixed period resets, an ARM can save you a bundle on interest. However, staying long term will likely lead to increased costs.

Pros of an adjustable-rate mortgage

- Lower initial monthly payments: With that lower rate also comes lower mortgage payments (at least during the introductory period). You can use the savings on other housing expenses or stash it away to put toward your future — and potentially higher — payments.
- Monthly payments might decrease: If prevailing market interest rates have gone down at the time your ARM resets, your monthly payment will also fall. However, some ARMs do set interest-rate floors, limiting how far the rate can decrease.

• Could be good for investors: An ARM can be appealing to investors who want to sell before the rate adjusts, or who will plan to put their savings on the interest into extra payments toward the principal.
• Flexibility to refinance: If you're nearing the end of your ARM's introductory term, you can opt to refinance to a fixed-rate mortgage to avoid potential interest rate hikes.

Cons of an adjustable-rate mortgage

• Monthly payments might increase: The biggest disadvantage (and biggest risk) of an ARM is the likelihood of your rate going up. If rates have risen since you took out the loan, your payments will increase when the loan resets. Often, there's a cap on the rate increase, but it can still sting and eat up more funds that you could use for other financial goals.
• More uncertainty in the long term: If you intend to keep the mortgage past the first rate reset, you'll need to plan for how you'll afford higher monthly payments long term. If you end up with an unaffordable payment, you could default, harm your credit and ultimately face foreclosure. If you need a stable monthly payment — or simply can't tolerate any level of risk — it's best to go with a fixed-rate mortgage.
• More complicated to prepay: Unlike a fixed-rate mortgage, adding extra to your monthly payment won't drastically shorten your loan term. This is because of how ARM interest rates are calculated. Instead, prepaying like this will have more of an effect on your monthly payment. If you want to shorten your term, you're better off paying in a large lump sum.
• Can be harder to qualify for: It can be more difficult to qualify for an ARM compared to a fixed-rate mortgage. You'll need a higher down payment of at least 5%, versus 3% for a conventional fixedrate loan. Plus, factors like your credit score, income and debt-to-income ratio can affect your ability to get an ARM.

How ARM rate caps limit your risk

One of the biggest misconceptions about ARMs is that your interest rate can jump without limits. ARMs typically have rate caps that limit how much your interest rate can increase. While rate caps don't eliminate the risk of higher payments, they do make that risk more predictable.

Look for those limits to be expressed in a rate structure, similar to 2/2/5. Think of these numbers like a guardrail that controls how much your interest rate can change over time. The first number tells you the highest the rate can increase at the first adjustment. The second number shows the maximum increase at each adjustment after that. The third number sets the highest your rate can ever go over the life of the loan.

For example, if you start with a 6.13% rate on a 5/1 ARM, a 2/2/5 cap means your rate couldn't rise above 8.13% at the first adjustment, no more than 10.13% at the next adjustment and never higher than 11.13% over the life of the loan.

In real dollars, using the National Association of Realtors' median existing-home price of $440,000 and assuming a 20% down payment, your loan amount would be about $352,000. At 6.13%, the monthly principal and interest payment would be roughly $2,140. If your rate increased to the first-adjustment cap of 8.13%, that payment would rise to about $2,615 — an increase of roughly $475 per month. While that's a meaningful jump, it's far less severe than it would be without rate caps in place.

So, why would a homebuyer choose an adjustable-rate mortgage?

• You don't plan to stay in the home for a long time. If you know you're going to sell a home within five to 10 years, you can opt for an ARM, taking advantage of its lower rate and payments, then sell before the rate adjusts.
• You plan to refinance. If you expect rates to drop before your ARM rate resets, taking out an ARM now and then refinancing to a lower rate at the right time could save you a considerable sum of money. Keep in mind, though, that if you refinance during the intro rate period, there are costs and fees to refinance.
• You're starting your career. Borrowers soon to leave school or early in their careers who know they'll earn substantially more over time might also benefit from the initial savings with an ARM. Ideally, your rising income would offset any payment increases.
• You're comfortable with the risk. If you're set on buying a home now with a lower payment to start, you might simply be willing to accept the risk that your rate and payments could rise down the line, whether or not you plan to move. "A borrower might perceive that the monthly savings between the ARM and fixed rates is worth the risk of a future increase in rate," says Pete Boomer, head of mortgage at Regions Bank in Birmingham, Alabama.

Why some buyers are choosing ARMs

In early 2022, both 30-year fixed mortgage rates and ARMs were near record lows. That same year, ARM applications reached a peak of 10.80%, according to the Mortgage Bankers Association (MBA). Even though 5/1 ARM rates hit their highest levels of the year in July 2026, buyers are still showing interest. ARM applications now account for 7.70% of mortgage applications.

Here are some of the reasons why ARMs are popular right now:
• Lower interest rates: As of the end of July 2026, the 5/1 ARM introductory rate is about a half point lower than 30year fixed mortgage rates. Lower rates give buyers more purchasing power — especially in markets where home prices remain high and affordability is a challenge.
• Ability to refinance: If you opt for an ARM for a lower initial rate and mortgage rates come down in the next few years, you can refinance to reduce your monthly payments further. You can also refinance to a fixed-rate mortgage if you want to keep that lower rate for the life of the loan. Check with your lender if it charges any fees to refinance during the initial rate period.
• Good option for some young families: ARMs tend to be more popular with younger, higher-income households with bigger mortgages, according to the Federal Reserve Bank of St. Louis. Higher-income households may be able to absorb the risk of higher payments when interest rates increase, and younger borrowers often have the time and potential earning power to weather the ups and downs of interest-rate trends compared to older borrowers.

Along with ARMs, you should consider a variety of loan types. Some may have a more lenient down payment requirement, lower interest rates or lower monthly payments than others.
• 15-year fixed-rate mortgage: If it's the interest rate you're worried about, consider a 15-year fixed-rate loan. It generally carries a lower rate than its 30-year counterpart. You'll make bigger monthly payments but pay less in interest and pay off your loan sooner.
• 30-year fixed-rate mortgage: If you want to keep those monthly payments low, a 30-year fixed mortgage is the way to go. You'll pay more in interest over the longer period, but your payments will be more manageable.

• Government-backed loans: If it's easier terms you crave, FHA, USDA or VA loans often come with lower down payments and looser qualifications.

Frequently asked questions

• How does an adjustable-rate mortgage work? An adjustable-rate mortgage has an initial fixed interest rate period, typically for three, five, seven or 10 years. Once that period ends, the interest rate adjusts at preset times, such as every six months or once per year, for the remainder of the loan term. Your new monthly payment can rise or fall along with the general mortgage rate trends.

• What are examples of ARM loans? The most common examples of adjustable-rate mortgages (ARMs) include 5/1, 7/1, and 10/1 ARMs. The first number tells you how many years your interest rate stays fixed, while the second number shows how often it can adjust after that. For example, 5/1 ARMs have fixed rates for the first five years which then change once a year based on current market interest rates. 10/1 ARMs operate similarly, except they have introductory periods for the first 10 years.

• How much can my ARM payment increase after the fixed period ends? Once your fixed-rate period ends, your interest rate and monthly payment can change if rates have gone up. The exact amount depends on your loan's adjustment caps, the index it follows and your lender's margin. Most ARMs include limits on how much your rate can increase at each adjustment and over the life of the loan, helping to prevent large payment increases.

• Is an adjustable-rate mortgage a bad idea right now? Not necessarily. An ARM can be a good choice if you plan to move, refinance or pay off the loan before the fixed-rate period ends due to the possibility for rising rates. If you want predictable monthly payments for the long term, a fixed-rate mortgage would be the better fit.