

MORGAN STANLEY EMERGING MARKETS DEBT FUND INC
Form N-CSR
March 08, 2010

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

FORM N-CSR

**CERTIFIED SHAREHOLDER REPORT OF REGISTERED
MANAGEMENT INVESTMENT COMPANIES**

Investment Company Act file number 811-07694

Morgan Stanley Emerging Markets Debt Fund, Inc.
(Exact name of registrant as specified in charter)

522 Fifth Avenue New York, NY
(Address of principal executive offices)

10036
(Zip code)

Randy Takian
522 Fifth Avenue New York, New York 10036
(Name and address of agent for service)

Registrant's telephone number, including area code: 1-800-231-2608

Date of fiscal year 12/31
end:

Date of reporting period: 12/31/09

Form N-CSR is to be used by management investment companies to file reports with the Commission not later than 10 days after the transmission to stockholders of any report that is required to be transmitted to stockholders under Rule 30e-1 under the Investment Company Act of 1940 (17 CFR 270.30e-1). The Commission may use the information provided on Form N-CSR in its regulatory, disclosure review, inspection, and policymaking roles.

A registrant is required to disclose the information specified by Form N-CSR, and the Commission will make this information public. A registrant is not required to respond to the collection of information contained in Form N-CSR unless the Form displays a currently valid Office of Management and Budget (OMB) control number. Please direct comments concerning the accuracy of the information collection burden estimate and any suggestions for reducing the burden to Secretary, Securities and Exchange Commission, 450 Fifth Street, NW, Washington, DC 20549-0609. The OMB has reviewed this collection of information under the clearance requirements of 44 U.S.C. Section 3507.

ITEM 1. REPORTS TO STOCKHOLDERS.

The Fund's annual report transmitted to shareholders pursuant to Rule 30e-1 under the Investment Company Act of 1940 is as follows:

INVESTMENT MANAGEMENT

Morgan Stanley

Emerging Markets Debt

Fund, Inc. (MSD)

Morgan Stanley

Investment Management Inc.

Investment Adviser

Annual Report

December 31, 2009

Morgan Stanley Emerging Markets Debt Fund, Inc.

Overview (unaudited)

Letter to Stockholders

Performance

For the year ended December 31, 2009, the Morgan Stanley Emerging Markets Debt Fund, Inc. (the Fund) had total returns of 36.18%, based on net asset value, and 52.55% based on market value per share (including reinvestment of distributions), compared to its benchmark, the J.P. Morgan Emerging Markets Bond Global Index (the Index), which returned 28.18%. On December 31, 2009, the closing price of the Fund's shares on the New York Stock Exchange was \$10.08, representing a 9.9% discount to the Fund's net asset value per share. Past performance is no guarantee of future results. Please keep in mind that high double-digit returns are highly unusual and cannot be sustained.

Factors Affecting Performance

- The first months of 2009 were characterized by unprecedented government intervention in the financial markets, with policy moves ranging from bank nationalizations to fiscal and monetary activism. Widespread easing of monetary policy announced by numerous governments around the world complemented this fiscal support, while monetary authorities that had limited scope for further rate cuts moved to quantitative easing. In addition, leaders from the G-20 pledged to support a package of measures which provided funding of more than \$1 trillion to contain the global downturn.
- The second quarter of 2009 was characterized by signs of a rebound in economic activity (green shoots) and increased risk appetite in the financial markets. Financial conditions improved and markets started to normalize. Emerging markets debt (EMD) staged a strong rally, benefiting from expectations that downside risks for the global economy had diminished. EMD fund flows turned positive after losing \$3.8 billion since the beginning of the year.
- This market normalization was driven by the massive injection of liquidity on the part of world's central banks, the sharp easing of monetary policy, and the recent stabilization of supply side variables such as industrial production. However, negative news at the global level, particularly from the demand side (retail sales, auto sales, exports, etc), still indicated that the real economy remained stressed and the recovery would likely be slow and fragile.

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- In the third and the last quarters of 2009, asset performance was supported by fundamentals. In this period, economic recovery was underway and financial risks diminished. However, trades in riskier assets that were popular during the rally months were crowded by investors and valuations were not that compelling. This was a period of consolidation, not only from an economic point of view (as economic recovery in systemically important countries consolidated) but also from an asset performance point of view, with returns moving toward more normal levels (that is, single digits or low double digits).

- EMD hard currency debt, as measured by the JP Morgan EMBI Global, returned 28.18% for the year ended December 31, 2009. External debt yields stood at 6.71%, with a spread of 294 basis points above U.S Treasuries as of December 31, 2009.

Morgan Stanley Emerging Markets Debt Fund, Inc.

Overview (unaudited)

Letter to Stockholders (cont d)

- Security selection in Ivory Coast and Russia aided to relative returns. Overweight positions in Kazakhstan and Venezuela also contributed. Conversely, security selection in Indonesia, an overweight exposure to Turkey and exposure to the Mexican peso detracted from relative returns.

Management Strategies

- Markets seem to keep building positions based on an optimistic growth outlook for EM for 2010. In addition, the environment is broadly constructive for EM currencies, which are supported by their higher carry and continued portfolio inflows. However, there should be a strong distinction between pricing assets for a more stable environment (our base case) and pricing assets for a strong growth environment. On average, our valuation models point to many EM credits being near fair value at current levels. We expect that some lower beta credits will be constrained by valuations and the strength in the EM corporate market to dissipate over the next few months. As such, we maintained overweights in select relatively lower credit quality countries experiencing positive rates of change. In addition, we see opportunities in select local currency markets where real rates are high and the currency undervalued.

Sincerely,

Randy Takian
President and Principal Executive Officer

January 2010

Morgan Stanley Emerging Markets Debt Fund, Inc.

December 31, 2009

Portfolio of Investments

(Showing Percentage of Total Value of Investments)

	Face Amount (000)	Value (000)
DEBT INSTRUMENTS (98.5%)		
Argentina (3.5%)		
Sovereign (3.5%)		
Republic of Argentina,		
1.68%, 8/3/12 (a)	\$ 8,305	\$ 7,628
8.28%, 12/31/33	1,787	1,344
		8,972
Brazil (14.1%)		
Sovereign (14.1%)		
Banco Nacional de Desenvolvimento Economico e Social,		
6.37%, 6/16/18 (b)	4,000	4,305
Federative Republic of Brazil,		
5.88%, 1/15/19 (c)	5,340	5,714
7.13%, 1/20/37	550	634
8.00%, 1/15/18	1,401	1,605
8.88%, 10/14/19 - 4/15/24	6,188	8,023
10.00%, 1/1/17	BRL 10,095	4,992
10.50%, 7/14/14	\$ 1,740	2,227
11.00%, 8/17/40 (c)	6,880	9,202
		36,702
Bulgaria (0.4%)		
Sovereign (0.4%)		
Republic of Bulgaria,		
8.25%, 1/15/15 (b)	898	1,053
Chile (0.5%)		
Sovereign (0.5%)		
Empresa Nacional de Petroleo,		
6.75%, 11/15/12 (b)	1,140	1,237
Colombia (3.8%)		
Sovereign (3.8%)		
Republic of Colombia,		
7.38%, 3/18/19	5,090	5,790
11.75%, 2/25/20	2,795	4,046
		9,836
Croatia (0.4%)		

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Sovereign (0.4%)		
Republic of Croatia,		
6.75%, 11/5/19 (b)	1,060	1,144
Dominican Republic (0.2%)		
Sovereign (0.2%)		
Dominican Republic,		
9.04%, 1/23/18	448	488
Ecuador (0.6%)		
Sovereign (0.6%)		
Republic of Ecuador,		
9.38%, 12/15/15	1,715	1,621
Georgia (0.3%)		
Sovereign (0.3%)		
Republic of Georgia,		
7.50%, 4/15/13	720	738
Ghana (0.8%)		
Sovereign (0.8%)		
Republic of Ghana,		
8.50%, 10/4/17 (b)	1,916	1,969
Indonesia (8.5%)		
Corporate (0.4%)		
Pindo Deli Finance Mauritius,		
Tranche A, Zero Coupon,		
4/28/15 (a)(b)(d)(e)	397	95
Tranche B, Zero Coupon,		
4/28/18 (a)(b)(d)(e)	1,707	213
Tranche C, Zero Coupon,		
4/28/25 (a)(b)(d)(e)	6,884	121
Tjiwi Kimia Finance Mauritius Ltd.,		
Tranche A, Zero Coupon,		
4/28/15 (a)(d)(e)	1,317	303
Tranche B, Zero Coupon,		
4/28/18 (a)(b)(d)(e)	1,477	258
Tranche C, Zero Coupon,		
4/28/27 (a)(b)(d)(e)	3,352	59
		1,049
Sovereign (8.1%)		
Republic of Indonesia,		
6.88%, 1/17/18	3,280	3,624
6.88%, 1/17/18 (b)	2,452	2,710
7.75%, 1/17/38	2,339	2,655
7.75%, 1/17/38 (b)	1,130	1,282
11.63%, 3/4/19	5,300	7,632
11.63%, 3/4/19 (b)	2,169	3,124
		21,027
		22,076

Morgan Stanley Emerging Markets Debt Fund, Inc.

December 31, 2009

Portfolio of Investments (cont d)

(Showing Percentage of Total Value of Investments)

	Face Amount (000)	Value (000)
Ivory Coast (0.4%)		
Sovereign (0.4%)		
Ivory Coast, Zero Coupon, 3/31/18 (e)	\$ 2,045	\$ 1,125
Kazakhstan (3.5%)		
Sovereign (3.5%)		
Intergas Finance BV, 6.38%, 5/14/17	610	576
KazMunaiGaz Finance Sub BV, 9.13%, 7/2/18	2,000	2,240
9.13%, 7/2/18 (b)	5,720	6,378
		9,194
Lithuania (0.4%)		
Sovereign (0.4%)		
Republic of Lithuania, 6.75%, 1/15/15 (b)	1,100	1,125
Mexico (12.6%)		
Sovereign (12.6%)		
Mexican Bonos, 8.50%, 11/18/38	MXN 69,250	5,160
10.00%, 12/5/24	25,810	2,266
Pemex Project Funding Master Trust, 1.55%, 6/15/10 (a)(b)	\$ 2,150	2,155
8.63%, 12/1/23	1,740	2,049
United Mexican States, 5.63%, 1/15/17 (c)	5,418	5,675
5.95%, 3/19/19	7,180	7,629
6.05%, 1/11/40	1,670	1,614
6.75%, 9/27/34 (c)	5,669	6,009
		32,557
Pakistan (0.4%)		
Sovereign (0.4%)		
Republic of Pakistan, 6.88%, 6/1/17	530	432
7.13%, 3/31/16	500	434
7.13%, 3/31/16 (b)	197	166
		1,032

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Panama (2.3%)

Sovereign (2.3%)

Republic of Panama,

5.20%, 1/30/20	2,100	2,116
7.13%, 1/29/26	1,140	1,291
8.88%, 9/30/27	430	561
9.38%, 4/1/29	1,523	2,033
		6,001

Peru (5.2%)

Sovereign (5.2%)

Republic of Peru,

7.13%, 3/30/19	1,360	1,571
7.35%, 7/21/25	3,360	3,864
8.75%, 11/21/33	6,130	7,999
		13,434

Philippines (4.5%)

Sovereign (4.5%)

Republic of Philippines,

8.38%, 6/17/19	1,041	1,267
8.88%, 3/17/15	2,608	3,175
9.00%, 2/15/13	2,240	2,610
9.50%, 2/2/30	3,409	4,543
		11,595

Qatar (0.7%)

Sovereign (0.7%)

State of Qatar (Registered),

9.75%, 6/15/30	1,260	1,783
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Russia (12.5%)

Sovereign (12.5%)

RSHB Capital S.A. for OJSC Russian Agricultural Bank,

6.30%, 5/15/17 (b)	2,004	2,028
7.18%, 5/16/13 (b)	1,920	2,045
Russian Federation,		
7.50%, 3/31/30 (b)(f)	831	941
Russian Federation (Registered),		
7.50%, 3/31/30 (c)(f)	18,042	20,546
12.75%, 6/24/28	4,000	6,820
		32,380

South Africa (0.2%)

Sovereign (0.2%)

Republic of South Africa,

6.88%, 5/27/19	470	530
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The accompanying notes are an integral part of the financial statements.

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Morgan Stanley Emerging Markets Debt Fund, Inc.

December 31, 2009

Portfolio of Investments (cont d)

(Showing Percentage of Total Value of Investments)

	Face Amount (000)	Value (000)
South Korea (1.6%)		
Sovereign (1.6%)		
Export-Import Bank of Korea, 5.88%, 1/14/15	\$ 1,760	\$ 1,893
Korea Development Bank, 8.00%, 1/23/14	1,320	1,522
Republic of Korea, 5.75%, 4/16/14	650	712
		4,127
Sri Lanka (0.4%)		
Sovereign (0.4%)		
Republic of Sri Lanka, 7.40%, 1/22/15 (b)	730	761
8.25%, 10/24/12	350	368
		1,129
Trinidad (0.8%)		
Sovereign (0.8%)		
National Gas Co. of Trinidad & Tobago Ltd., 6.05%, 1/15/36 (b)	2,369	2,154
Turkey (10.1%)		
Sovereign (10.1%)		
Republic of Turkey, Zero Coupon, 5/11/11	TRY 8,040	4,815
6.75%, 4/3/18	\$ 2,845	3,101
6.88%, 3/17/36	1,174	1,200
7.50%, 7/14/17 - 11/7/19	3,856	4,379
8.00%, 2/14/34	867	1,006
11.00%, 1/14/13	1,445	1,745
11.00%, 8/6/14	TRY 3,310	2,264
11.50%, 1/23/12	\$ 320	375
11.88%, 1/15/30	3,237	5,244
16.00%, 3/7/12	TRY 2,740	2,066
		26,195
Ukraine (0.7%)		
Sovereign (0.7%)		
Ukraine Government, 6.58%, 11/21/16	\$ 836	648

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6.75%, 11/14/17	120	92
7.65%, 6/11/13	1,096	945
		1,685
Uruguay (0.2%)		
Sovereign (0.2%)		
Republic of Uruguay,		
8.00%, 11/18/22	545	627
Venezuela (8.9%)		
Sovereign (8.9%)		
Republic of Venezuela,		
5.75%, 2/26/16	987	646
6.00%, 12/9/20	1,210	669
7.00%, 3/31/38	1,631	905
7.65%, 4/21/25	2,700	1,600
9.00%, 5/7/23	1,197	811
9.25%, 9/15/27 - 5/7/28	15,582	11,025
10.75%, 9/19/13	8,330	7,372
		23,028
TOTAL DEBT INSTRUMENTS (Cost \$242,784)		255,537

	No. of	
	Warrants	
WARRANTS (0.2%)		
Nigeria (0.1%)		
Central Bank of Nigeria, expires 11/15/20 (a)(d)	2,250	259
Venezuela (0.1%)		
Republic of Venezuela, Oil-Linked Payment Obligation, expires 4/15/20 (a)(d)	4,500	121
TOTAL WARRANTS (Cost \$ @)		380

	Shares	
SHORT-TERM INVESTMENT (1.3%)		
United States (1.3%)		
Investment Company (1.3%)		
Morgan Stanley Institutional Liquidity Funds Money Market Portfolio Institutional Class (g)		
(Cost \$3,491)	3,490,844	3,491
TOTAL INVESTMENTS (100.0%) (Cost \$246,275)		259,408
LIABILITIES IN EXCESS OF OTHER ASSETS		(24,959)
NET ASSETS		\$ 234,449

6 The accompanying notes are an integral part of the financial statements.

Morgan Stanley Emerging Markets Debt Fund, Inc.

December 31, 2009

Portfolio of Investments (cont d)

- (a) Variable/Floating Rate Security Interest rate changes on these instruments are based on changes in a designated base rate. The rates shown are those in effect on December 31, 2009.
- (b) 144A security Certain conditions for public sale may exist. Unless otherwise noted, these securities are deemed to be liquid.
- (c) Denotes all or a portion of securities subject to repurchase under the Reverse Repurchase Agreements as of December 31, 2009.
- (d) Security has been deemed illiquid at December 31, 2009.
- (e) Issuer is in default.
- (f) Step Bond Coupon rate increases in increments to maturity. Rate disclosed is as of December 31, 2009. Maturity date disclosed is the ultimate maturity date.
- (g) See Note G within the Notes to Financial Statements regarding investment in Morgan Stanley Institutional Liquidity Funds Money Market Portfolio Institutional Class.
- @ Value is less than \$500.

Foreign Currency Exchange Contracts Information:

The Fund had the following foreign currency exchange contract(s) open at period end:

Currency to Deliver (000)		Value (000)	Settlement Date	In Exchange For (000)		Value (000)	Net Unrealized Appreciation (Depreciation) (000)
MXN	4,697	\$359	1/4/10	USD	361	\$361	\$2
USD	4,575	4,575	1/28/10	KRW	5,406,000	4,639	64
USD	2,368	2,368	3/24/10	RUB	72,510	2,362	(6)
		\$7,302				\$7,362	\$60

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BRL Brazilian Real

KRW Korean Won

MXN Mexican Peso

RUB Russian Ruble

TRY Turkish Lira

USD United States Dollar

Futures Contracts:

The Fund had the following futures contract(s) open at period end:

	Number of Contracts	Value (000)	Expiration Date	Net Unrealized Appreciation (Depreciation) (000)
Short:				
U.S. Treasury 10 yr. Note	237	\$27,362	Mar-10	\$709

Fair Value Measurement Information:

The following is a summary of the inputs used to value the Fund's net assets as of December 31, 2009. (See Note A-7 to the financial statements for further information regarding fair value measurement.)

Investment Type	Level 1 Quoted prices (000)	Level 2 Other significant observable inputs (000)	Level 3 Significant unobservable inputs (000)	Total (000)
Assets:				
Debt Instruments				
Industrials	\$	\$ 1,049	\$	\$ 1,049
Sovereign		254,488		254,488
Total Debt Instruments		255,537		255,537
Foreign Currency Exchange Contracts		66		66
Futures Contracts	709			709
Short-Term Investment				
Investment Company	3,491			3,491
Warrants		380		380
Total Assets	4,200	255,983		260,183

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Liabilities:

Foreign Currency Exchange Contracts			6		6
Reverse Repurchase Agreement			25,903		25,903
Total Liabilities			25,909		25,909
Total	\$	4,200	\$	230,074	\$ 234,274

The accompanying notes are an integral part of the financial statements.

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Morgan Stanley Emerging Markets Debt Fund, Inc.

December 31, 2009

Portfolio of Investments (cont d)

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Portfolio Composition

Classification	Percentage of	
	Total Investments	
Sovereign	98.3	%
Other*	0.4	
Short-Term Investment	1.3	
Total Investments	100.0	%

* Industries representing less than 5% of total investments.

8 The accompanying notes are an integral part of the financial statements.

Morgan Stanley Emerging Markets Debt Fund, Inc.

December 31, 2009

Financial Statements

Statement of Assets and Liabilities

December 31, 2009
(000)

Assets:

Investments in Securities of Unaffiliated Issuers, at Value (Cost \$242,784)	\$255,917
Investment in Security of Affiliated Issuer, at Value (Cost \$3,491)	3,491
Total Investments in Securities, at Value (Cost \$246,275)	259,408
Interest Receivable	5,321
Foreign Currency, at Value (Cost \$677)	687
Due from Broker	473
Receivable for Lehman Brothers Closed Reverse Repurchase Transactions	183
Unrealized Appreciation on Foreign Currency Exchange Contracts	66
Receivable from Affiliate	@
Dividends Receivable	@
Other Assets	6
Total Assets	266,144

Liabilities:

Payable For:	
Reverse Repurchase Agreements	25,914
Dividends Declared	5,510
Investment Advisory Fees	201
Professional Fees	27
Administration Fees	7
Custodian Fees	6
Directors' Fees and Expenses	@
Unrealized Depreciation on Foreign Currency Exchange Contracts	6
Other Liabilities	24
Total Liabilities	31,695

Net Assets

Applicable to 20,943,315 Issued and Outstanding \$0.01 Par Value Shares (100,000,000 Shares Authorized) \$234,449

Net Asset Value Per Share \$ 11.19

Net Assets Consist of:

Common Stock	\$ 209
Paid-in Capital	230,044
Distributions in Excess of Net Investment Income	(1,811)
Accumulated Net Realized Loss	(7,914)
Unrealized Appreciation (Depreciation) on Investments, Futures Contracts and Foreign Currency Exchange Contracts and Translations	13,921
Net Assets	\$ 234,449

@ Amount is less than \$500.

The accompanying notes are an integral part of the financial statements.

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Morgan Stanley Emerging Markets Debt Fund, Inc.

December 31, 2009

Financial Statements (cont d)

	Year Ended December 31, 2009 (000)
Statement of Operations	
Investment Income:	
Interest from Securities of Unaffiliated Issuers (Net of \$3 Foreign Taxes Withheld)	\$18,594
Dividends from Security of Affiliated Issuer	8
Total Investment Income	18,602
Expenses:	
Investment Advisory Fees (Note B)	2,127
Administration Fees (Note C)	170
Professional Fees	105
Stockholder Reporting Expenses	32
Custodian Fees (Note D)	26
Stockholder Servicing Agent Fees	9
Directors' Fees and Expenses	6
Other Expenses	30
Expenses Before Non Operating Expenses	2,505
Interest Expense on Reverse Repurchase Agreements	152
Reorganization Expense (Note J)	15
Bank Overdraft Expense	@
Total Expenses	2,672
Waiver of Administration Fees (Note C)	(94)
Rebate from Morgan Stanley Affiliates (Note G)	(4)
Expense Offset (Note D)	@
Net Expenses	2,574
Net Investment Income	16,028
Net Realized Gain (Loss) on:	
Investments	1,453
Foreign Currency Exchange Contracts	123
Foreign Currency Transactions	(3,391)
Futures Contracts	(617)
Net Realized Loss	(2,432)
Change in Unrealized Appreciation (Depreciation) on:	
Investments	48,882
Foreign Currency Exchange Contracts	85
Foreign Currency Translations	133
Future Contracts	709
Change in Unrealized Appreciation (Depreciation)	49,809
Net Realized Loss and Change in Unrealized Appreciation (Depreciation)	47,377
Net Increase in Net Assets Resulting from Operations	\$63,405

@ Amount is less than \$500.

10 The accompanying notes are an integral part of the financial statements.

Morgan Stanley Emerging Markets Debt Fund, Inc.

December 31, 2009

Financial Statements (cont d)

	Year Ended December 31, 2009 (000)	Year Ended December 31, 2008 (000)
Statements of Changes in Net Assets		
Increase (Decrease) in Net Assets		
Operations:		
Net Investment Income	\$ 16,028	\$ 13,913
Net Realized Loss	(2,432)	(2,664)
Net Change in Unrealized Appreciation (Depreciation)	49,809	(47,040)
Net Increase (Decrease) in Net Assets Resulting from Operations	63,405	(35,791)
Distributions from and/or in Excess of:		
Net Investment Income	(13,364)	(18,360)
Capital Share Transactions:		
Repurchase of Shares (173,000 and 699,771 shares)	(1,298)	(5,974)
Total Increase (Decrease)	48,743	(60,125)
Net Assets:		
Beginning of Period	185,706	245,831
End of Period (Including Distributions in Excess of Net Investment Income of \$(1,811) and \$(1,020))	\$234,449	\$185,706

The accompanying notes are an integral part of the financial statements.

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Morgan Stanley Emerging Markets Debt Fund, Inc.

December 31, 2009

Financial Statements (cont d)

	Year Ended December 31, 2009 (000)
Statement of Cash Flows	
Cash Flows From Operating Activities:	
Proceeds from Sales and Maturities of Long-Term Investments	\$ 190,526
Purchase of Long-Term Investments	(198,281)
Net (Increase) Decrease in Short-Term Investments	4,171
Net (Increase) Decrease in Foreign Currency Holdings	(198)
Net Increase (Decrease) in Cash Overdrafts	(137)
Net Realized Gain (Loss) for Foreign Currency Transactions	(3,268)
Net Realized Gain (Loss) on Futures Contracts	(617)
Net Investment Income	16,028
Adjustments to Reconcile Net Investment Income to Net Cash Provided (Used) by Operating Activities:	
Net (Increase) Decrease in Receivables Related to Operations	(164)
Net (Increase) Decrease in Payables Related to Operations	(51)
Accretion/Amortization of Discounts and Premiums	92
Net Cash Provided (Used) by Operating Activities	8,101
Cash Flows From Financing Activities:	
Cash Received for Reverse Repurchase Agreements	80,358
Cash Paid for Reverse Repurchase Agreements	(70,918)
Payment for Fund Shares Repurchased	(1,298)
Cash Distribution Paid	(16,243)
Net Cash Provided (Used) for Financing Activities	(8,101)
Net Increase (Decrease) in Cash	
Cash at Beginning of Period	
Cash at End of Period	\$
Supplemental Disclosure of Cash Flow Information:	
Interest Paid on Reverse Repurchase Agreements during the Period	\$ 145

Morgan Stanley Emerging Markets Debt Fund, Inc.

December 31, 2009

Financial Highlights

Selected Per Share Data and Ratios

	Year Ended December 31,				
	2009	2008	2007	2006	2005
Net Asset Value, Beginning of Period	\$ 8.79	\$ 11.27	\$ 11.19	\$ 10.80	\$ 10.39
Net Investment Income	0.76	0.65	0.69	0.67	0.91
Net Realized and Unrealized Gain (Loss) on Investments	2.27	(2.32)	0.03	0.49	0.44
Total from Investment Operations	3.03	(1.67)	0.72	1.16	1.35
Distributions from and/or in excess of:					
Net Investment Income	(0.64)	(0.86)	(0.66)	(0.77)	(0.94)
Anti-Dilutive Effect of Share Repurchase Program	0.01	0.05	0.02		
Net Asset Value, End of Period	\$ 11.19	\$ 8.79	\$ 11.27	\$ 11.19	\$ 10.80
Per Share Market Value, End of Period	\$ 10.08	\$ 7.07	\$ 9.70	\$ 10.84	\$ 10.88
TOTAL INVESTMENT RETURN:					
Market Value	52.55%	(18.74)%	(4.52)%	7.38%	23.98%
Net Asset Value(1)	36.18%	(12.95)%	7.46%	11.66%	13.83%
RATIOS, SUPPLEMENTAL DATA:					
Net Assets, End of Period (Thousands)	\$234,449	\$185,706	\$245,831	\$246,684	\$238,091
Ratio of Expenses to Average Net Assets(2)	1.21%+	1.23%+	1.29%+	1.34%	1.36%
Ratio of Expenses to Average Net Assets Excluding Non Operating Expenses	1.13%+	1.15%+	1.10%+	1.16%	1.16%
Ratio of Net Investment Income to Average Net Assets(2)	7.54%+	6.19%+	6.11%+	6.12%	8.58%
Ratio of Rebate from Morgan Stanley Affiliates to Average Net Assets	0.00%\$	0.00%\$	0.00%\$	N/A	N/A
Portfolio Turnover Rate	83%	64%	56%	44%	50%
(2) Supplemental Information on the Ratios to Average Net Assets:					
Ratios Before Expenses Waived by Administrator:					
Ratio of Expenses to Average Net Assets	1.26%+	1.28%+	1.34%+	1.38%	1.41%
Ratio of Net Investment Income to Average Net Assets	7.49%+	6.14%+	6.06%+	6.08%	8.53%

(1) Total investment return based on net asset value per share reflects the effects of changes in net asset value on the performance of the Fund during each period, and assumes dividends and distributions, if any, were reinvested. This percentage is not an indication of the performance of a stockholder's investment in the Fund based on market value due to differences between the market price of the stock and the net asset value per share of the Fund.

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Per share amount is based on average shares outstanding.

§ Amount is less than 0.005%

+ The Ratios of Expenses and Net Investment Income reflect the rebate of certain Fund expenses in connection with the investments in Morgan Stanley affiliates during the period. The effect of the rebate on the ratios is disclosed in the above table as Ratio of Rebate from Morgan Stanley Affiliates to Average Net Assets .

The accompanying notes are an integral part of the financial statements.

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Morgan Stanley Emerging Markets Debt Fund, Inc.

December 31, 2009

Notes to Financial Statements

Morgan Stanley Emerging Markets Debt Fund, Inc. (the Fund) was incorporated in Maryland on May 6, 1993, and is registered as a non-diversified, closed-end management investment company under the Investment Company Act of 1940, as amended (the 1940 Act). The Fund's primary investment objective is to produce high current income and as a secondary objective, to seek capital appreciation, through investments primarily in debt securities of government and government-related issuers located in emerging countries, of entities organized to restructure outstanding debt of such issuers and debt securities of corporate issuers located in or organized under the laws of emerging countries. To the extent that the Fund invests in derivative instruments that the Adviser believes have economic characteristics similar to debt securities of government and government-related issuers located in emerging market countries and of entities organized to restructure outstanding debt of such issuers, such investments will be counted for purposes of the Fund's policy in the previous sentence. To the extent the Fund makes such investments, the Fund will be subject to the risks of such derivative instruments as described herein.

A. Significant Accounting Policies: The following significant accounting policies are in conformity with U.S. generally accepted accounting principles. Such policies are consistently followed by the Fund in the preparation of its financial statements. U.S. generally accepted accounting principles may require management to make estimates and assumptions that affect the reported amounts and disclosures in the financial statements. Actual results may differ from those estimates.

1. Security Valuation: Bonds and other fixed income securities may be valued according to the broadest and most representative market. In addition, bonds and other fixed income securities may be valued on the basis of prices provided by a pricing service. The prices provided by a pricing service take into account broker dealer market price quotations for institutional size trading in similar groups of securities, security quality, maturity, coupon and other security characteristics as well as any developments related to the specific securities. Securities listed on a foreign exchange are valued at their closing price. Unlisted securities and listed securities not traded on the valuation date for which market quotations are readily available are valued at the mean between the current bid and asked prices obtained from reputable brokers. Equity securities listed on a U.S. exchange are valued at the latest quoted sales price on the valuation date. Equity securities listed or traded on NASDAQ, for which market quotations are available, are valued at the NASDAQ Official Closing Price. Debt securities purchased with remaining maturities of 60 days or less are valued at amortized cost, unless the Board of Directors (the Directors) determine such valuation does not reflect the securities' market value, in which case these securities will be valued at their fair value as determined by the Directors.

All other securities and investments for which market values are not readily available, including restricted securities, and those securities for which it is inappropriate to determine prices in accordance with the aforementioned procedures, are valued at fair value as determined in good faith under procedures adopted by the Directors, although the actual calculations may be done by others. Factors considered in making this determination may include, but are not limited to, information obtained by contacting the issuer, analysts, or the appropriate stock exchange (for exchange-traded securities), analysis of the issuer's financial statements or other available documents and, if necessary, available information concerning other securities in similar circumstances.

Most foreign markets close before the New York Stock Exchange (NYSE). Occasionally, developments that could affect the closing prices of securities and other assets may occur between the times at which valuations of such

Morgan Stanley Emerging Markets Debt Fund, Inc.

December 31, 2009

Notes to Financial Statements (cont d)

securities are determined (that is, close of the foreign market on which the securities trade) and the close of business on the NYSE. If these developments are expected to materially affect the value of the securities, the valuations may be adjusted to reflect the estimated fair value as of the close of the NYSE, as determined in good faith under procedures established by the Directors.

2. Reverse Repurchase Agreements: The Fund may enter into reverse repurchase agreements with institutions that the Fund's investment adviser has determined are creditworthy. Under a reverse repurchase agreement, the Fund sells securities and agrees to repurchase them at a mutually agreed upon date and price. Reverse repurchase agreements involve the risk that the market value of the securities purchased with the proceeds from the sale of securities received by the Fund may decline below the price of the securities the Fund is obligated to repurchase. Reverse repurchase agreements also involve credit risk with the counterparty to the extent that the value of securities subject to repurchase exceed the Fund's liability under the reverse repurchase agreement. Securities subject to repurchase under reverse repurchase agreements, if any, are designated as such in the Portfolio of Investments.

At December 31, 2009, the Fund had a reverse repurchase agreement outstanding with UBS as follows:

	Maturity in Less than 365 Days
Value of Securities Subject to Repurchase	\$28,776,000
Liability Under Reverse Repurchase Agreement	\$25,914,000
Weighted Average Days to Maturity	81.29

The weighted average weekly balance of reverse repurchase agreements outstanding during the year ended December 31, 2009 was approximately \$21,491,000 at a weighted average weekly interest rate of 0.69%.

3. Foreign Currency Translation: The books and records of the Fund are maintained in U.S. dollars. Foreign currency amounts are translated into U.S. dollars at the mean of the bid and asked prices of such currencies against U.S. dollars last quoted by a major bank as follows:

investments, other assets and liabilities at the prevailing rates of exchange on the valuation date;

investment transactions and investment income at the prevailing rates of exchange on the dates of such transactions.

Although the net assets of the Fund are presented at the foreign exchange rates and market values at the close of the period, the Fund does not isolate that portion of the results of operations arising as a result of changes in the foreign exchange rates from the fluctuations arising from changes in the market prices of the securities held at period end. Similarly, the Fund does not isolate the effect of changes in foreign exchange rates from the fluctuations arising from changes in the market prices of securities sold during the period. Accordingly, realized and unrealized foreign currency gains (losses) on investments in securities are included in the reported net realized and unrealized gains (losses) on investment transactions and balances.

Net realized gains (losses) on foreign currency transactions represent net foreign exchange gains (losses) from sales and maturities of foreign currency exchange contracts, disposition of foreign currencies, currency gains or losses realized between the trade and settlement dates on securities transactions, and the difference between the amount of investment income and foreign withholding taxes recorded on the Fund's books and the U.S. dollar equivalent amounts actually received or paid. Net unrealized currency gains (losses) from valuing foreign currency denominated assets and liabilities at period end exchange rates are reflected as a component of unrealized

Morgan Stanley Emerging Markets Debt Fund, Inc.

December 31, 2009

Notes to Financial Statements (cont d)

appreciation (depreciation) on investments and foreign currency translations in the Statement of Assets and Liabilities. The change in unrealized currency gains (losses) on foreign currency translations for the period is reflected in the Statement of Operations.

A significant portion of the Fund's net assets consist of securities of issuers located in emerging markets or which are denominated in foreign currencies. Such investments may be concentrated in a limited number of countries and regions and may vary throughout the year. Changes in currency exchange rates will affect the value of and investment income from foreign currency denominated securities. Emerging market securities are often subject to greater price volatility, limited capitalization and liquidity, and higher rates of inflation than U.S. securities. In addition, emerging market securities may be subject to substantial governmental involvement in the economy and greater social, economic and political uncertainty.

4. Derivatives: The Fund may use derivative instruments for a variety of purposes, including hedging, risk management, portfolio management or to earn income. Derivatives are financial instruments whose value is based on the value of another underlying asset, interest rate, index or financial instrument. A derivative instrument often has risks similar to its underlying instrument and may have additional risks, including imperfect correlation between the value of the derivative and the underlying instrument, risks of default by the other party to certain transactions, magnification of losses incurred due to changes in the market value of the securities, instruments, indices or interest rates to which they relate, and risks that the transactions may not be liquid. The use of derivatives involves risks that are different from, and possibly greater than, the risks associated with other portfolio investments. Derivatives may involve the use of highly specialized instruments that require investment techniques and risk analyses different from those associated with other portfolio investments. All of the Fund's portfolio holdings, including derivative instruments, are marked to market each day with the change in value reflected in unrealized appreciation (depreciation). Upon disposition, a realized gain or loss is generally recognized.

Certain derivative transactions may give rise to a form of leverage. Leverage associated with derivative transactions may cause the Fund to liquidate portfolio positions when it may not be advantageous to do so to satisfy its obligations or to meet earmarking or segregation requirements, pursuant to applicable SEC rules and regulations, or may cause the Fund to be more volatile than if the Fund had not been leveraged. Although the Investment Adviser seeks to use derivatives to further the Fund's investment objectives, there is no assurance that the use of derivatives will achieve this result.

Following is a description of the derivative instruments and techniques that the Fund may use and their associated risks:

Futures: In respect to futures, the Fund is subject to equity risk, interest rate risk and foreign currency exchange risk in the normal course of pursuing its investment objectives. A futures contract is a standardized agreement between two parties to buy or sell a specific quantity of an underlying instrument at a specific price at a specific future time. The value of a futures contract tends to increase and decrease in tandem with the value of the underlying instrument. Futures contracts are bilateral agreements, with both the purchaser and the seller equally obligated to complete the transaction. Depending on the terms of the particular contract, futures contracts are settled through either physical delivery of the underlying instrument on the settlement date or by payment of a cash settlement amount on the settlement date. During the period the futures contract is open, payments are received from or made to

Morgan Stanley Emerging Markets Debt Fund, Inc.

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Notes to Financial Statements (cont d)

the broker based upon changes in the value of the contract (the variation margin). The risk of loss associated with a futures contract is in excess of the variation margin reflected as part of Due from (to) Broker on the Statement of Assets and Liabilities. A decision as to whether, when and how to use futures involves the exercise of skill and judgment and even a well conceived futures transaction may be unsuccessful because of market behavior or unexpected events. In addition to the derivatives risks discussed above, the prices of futures can be highly volatile, using futures can lower total return, and the potential loss from futures can exceed the Fund's initial investment in such contracts.

Options: In respect to options, the Fund is subject to equity risk, interest rate risk and foreign currency exchange risk in the normal course of pursuing its investment objectives. If a Fund buys an option, it buys a legal contract giving it the right to buy or sell a specific amount of the underlying instrument or futures contract on the underlying instrument such as a security, currency or index, at an agreed upon price typically in exchange for a premium paid by the Fund. The Fund may purchase put and call options. Purchasing call options tends to increase the Fund's exposure to the underlying (or similar) instrument. Purchasing put options tends to decrease the Fund's exposure to the underlying (or similar) instrument. When entering into purchased option contracts, the Fund bears the risk of interest or exchange rates or securities prices moving unexpectedly, in which case, the Fund may not achieve the anticipated benefits of the purchased option contracts; however the risk of loss is limited to the premium paid. Purchased options are reported as part of Total Investments on the Statement of Assets and Liabilities. Premium paid for purchasing options which expired are treated as realized losses. If a Fund sells an option, it sells to another party the right to buy from or sell to the Fund a specific amount of the underlying instrument or futures contract on the underlying instrument at an agreed upon price typically in exchange for a premium received by the Fund. The Fund may write call and put options on stock indexes, futures, securities or currencies it owns or in which it may invest. Writing put options tend to increase the Fund's exposure to the underlying instrument. Writing a call options tend to decrease the Fund's exposure to the underlying instruments. When the Fund writes a call or put option, an amount equal to the premium received is recorded as a liability. Any liability recorded is subsequently adjusted to reflect the current value of the options written. Premiums received from writing options which expire are treated as realized gains. Premiums received from writing options which are exercised or are closed are added to or offset against the proceeds or amount paid on the transaction to determine the net realized gain or loss. The Fund as a writer of an option has no control over whether the underlying future, security or currency may be sold (call) or purchased (put) and as a result bears the market risk of an unfavorable change in the price of the future, security or currency underlying the written option. There is the risk the Fund may not be able to enter into a closing transaction because of an illiquid market. A decision as to whether, when and how to use options involves the exercise of skill and judgment and even a well conceived option transaction may be unsuccessful because of market behavior or unexpected events. The prices of options can be highly volatile and the use of options can lower total returns.

Swaps: In respect to swaps, the Fund is subject to equity risk, interest rate risk and credit risk in the normal course of pursuing its investment objectives. A swap agreement is an agreement between two parties pursuant to which the parties exchange payments at specified dates on the basis of a specified notional amount, with the payments calculated by reference to specified securities, indexes, reference rates,

Morgan Stanley Emerging Markets Debt Fund, Inc.

December 31, 2009

Notes to Financial Statements (cont d)

currencies or other instruments. Most swap agreements provide that when the period payment dates for both parties are the same, the payments are made on a net basis (i.e., the two payment streams are netted out, with only the net amount paid by one party to the other). The Fund's obligations or rights under a swap agreement entered into on a net basis will generally be equal only to the net amount to be paid or received under the agreement, based on the relative values of the positions held by each counterparty. In a zero-coupon interest rate swap, payment only occurs at maturity, at which time one counterparty pays the total compounded fixed rate over the life of the swap and the other pays the total compounded floating rate that would have been earned had a series of floating rate investments been rolled over through the life of the swap. Swap agreements are not entered into or traded on exchanges and there is no central clearing or guaranty function for swaps. Therefore, swaps are subject to credit risk or the risk of default or non-performance by the counterparty. Swaps could result in losses if interest rate or foreign currency exchange rates or credit quality changes are not correctly anticipated by the Fund or if the reference index, security or investments do not perform as expected. When the Fund has an unrealized loss on a swap agreement, the Fund has instructed the custodian to pledge cash or liquid securities as collateral with a value approximately equal to the amount of the unrealized loss. Collateral pledges are monitored and subsequently adjusted if and when the swap valuations fluctuate. Cash collateral is included with Due from (to) Broker on the Statement of Assets and Liabilities. Cash collateral has been offset against open swap agreements under the provisions of Financial Accounting Standards Board (FASB) Accounting Standards Codification(TM) (ASC) Balance Sheet (ASC 210) (formerly known as FIN 39). Offsetting of Amounts Related to Certain Contracts an interpretation of ASC 210-20 (formerly known as APB No. 10 and SFAS 105) and are included within Swap Agreements, at Value on the Statement of Assets and Liabilities. For cash collateral received, the Fund pays a monthly fee to the counterparty based on the effective rate for Federal Funds. This fee, when paid, is included within realized gain (loss) on swap agreements on the Statement of Operations.

The Fund adopted the provisions of the FASB ASC 815-10, Derivatives and Hedging (ASC 815-10) (formerly known as SFAS 133-1) and ASC 460-10, Guarantees (ASC 460-10) (formerly known as FIN 45-4): An Amendment of FASB ASC 815 (formerly known as SFAS 133) and ASC 460 (formerly known as FIN 45), effective November 30, 2008. ASC 815-10 and ASC 460-10 requires the seller of credit derivatives to provide additional disclosure about its credit derivatives. The Fund's use of swaps may include those based on the credit of an underlying security and commonly referred to as credit default swaps. Where the Fund is the buyer of a credit default swap agreement, it would be entitled to receive the par (or other agreed-upon) value of a referenced debt obligation from the counterparty to the agreement only in the event of a default by a third party on the debt obligation. If no default occurs, the Fund would have paid to the counterparty a periodic stream of payments over the term of the agreement and received no benefit from the agreement. When the Fund is the seller of a credit default swap agreement, it receives the stream of payments but is obligated to pay upon default of the referenced debt obligation. The current credit rating of each individual issuer is listed in the table following the Portfolio of Investments and serves as an indicator of the current status of the payment/performance risk of the credit derivative. Alternatively, for credit default swaps on an index of credits, the quoted market prices and current values serve as an indicator of the current status of the payment/performance risk of the credit derivative. Generally, lower credit ratings and increasing market values, in absolute terms, represent a deterioration of the credit and a greater likelihood of an adverse credit event of the issuer.

Morgan Stanley Emerging Markets Debt Fund, Inc.

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Notes to Financial Statements (cont d)

Upfront payments received or paid by the Fund will be reflected as an asset or liability on the Statement of Assets and Liabilities.

Structured Investments: The Fund also may invest a portion of its assets in structured notes and other types of structured investments. A structured note is a derivative security for which the amount of principal repayment and/or interest payments is based on the movement of one or more factors. These factors include, but are not limited to, currency exchange rates, interest rates (such as the prime lending rate or LIBOR), referenced bonds and stock indices. Investments in structured notes involve risks including interest rate risk, credit risk and market risk. Changes in interest rates and movement of the factor may cause significant price fluctuations and changes in the reference factor may cause the interest rate on the structured note to be reduced to zero and any further changes in the reference factor may then reduce the principal amount payable on maturity. Other types of structured investments include interests in entities organized and operated for the purpose of restructuring the investment characteristics of underlying investment interests or securities. These investment entities may be structured as trusts or other types of pooled investment vehicles. Holders of structured investments bear risks of the underlying investment and are subject to counterparty risk. Certain structured investments may be thinly traded or have a limited trading market and may have the effect of increasing the Fund's illiquidity to the extent that the Fund, at a particular point in time, may be unable to find qualified buyers for these securities.

Foreign Currency Forward Contracts: In connection with its investments in foreign securities, the Fund also may enter into contracts with banks, brokers or dealers to purchase or sell securities or foreign currencies at a future date (forward contracts). A foreign currency forward contract is a negotiated agreement between the contracting parties to exchange a specified amount of currency at a specified future time at a specified rate. The rate can be higher or lower than the spot rate between the currencies that are the subject of the contract. Forward foreign currency exchange contracts may be used to protect against uncertainty in the level of future foreign currency exchange rates or to gain or modify exposure to a particular currency. In addition, the Fund may use cross currency hedging or proxy hedging with respect to currencies in which the Fund has or expects to have portfolio or currency exposure. Cross currency hedges involve the sale of one currency against the positive exposure to a different currency and may be used for hedging purposes or to establish an active exposure to the exchange rate between any two currencies. A currency exchange contract is marked-to-market daily and the change in market value is recorded by the Fund as unrealized gain or loss. The Fund records realized gains (losses) when the contract is closed equal to the difference between the value of the contract at the time it was opened and the value at the time it was closed. Hedging the Fund's currency risks involves the risk of mismatching the Fund's objectives under a forward or futures contract with the value of securities denominated in a particular currency. Furthermore, such transactions reduce or preclude the opportunity for gain if the value of the currency should move in the direction opposite to the position taken. There is an additional risk to the effect that currency contracts create exposure to currencies in which the Fund's securities are not denominated. Unanticipated changes in currency prices may result in poorer overall performance for the Fund than if it had not entered into such contracts.

Over-the-Counter Trading: Securities and other derivative instruments that may be purchased or sold by the Fund may consist of instruments not traded on an exchange. The risk of nonperformance by the obligor on such an instrument may be greater, and the ease with which the Fund can dispose of or enter into closing transactions with respect to such an instrument may be less, than in the case of

Morgan Stanley Emerging Markets Debt Fund, Inc.

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Notes to Financial Statements (cont d)

an exchange-traded instrument. In addition, significant disparities may exist between bid and ask prices for derivative instruments that are not traded on an exchange. Derivative instruments not traded on exchanges are also not subject to the same type of government regulation as exchange traded instruments, and many of the protections afforded to participants in a regulated environment may not be available in connection with such transactions.

The Fund adopted the provisions of FASB ASC 815, Derivatives and Hedging: Overall (ASC 815) (formerly known as SFAS 161), effective December 31, 2008. ASC 815 is intended to improve financial reporting about derivative instruments by requiring enhanced disclosures to enable investors to better understand how and why the Fund uses derivative instruments, how these derivative instruments are accounted for and their effects on the Fund's financial position and results of operations.

The following table sets forth the fair value of the Fund's derivative contracts by primary risk exposure as of December 31, 2009.

Primary Risk Exposure	Statement of Assets and Liabilities	Foreign Currency Exchange Contracts (000)	Futures Contracts (000)(a)
Assets:			
Foreign Currency Contracts Risk	Receivables	\$66	\$
Interest Rate Contracts	Receivables		709
Total Receivables		\$66	\$709
Liabilities:			
Foreign Currency Contracts Risk	Payables	\$ 6	\$

(a) This amount represents the cumulative appreciation (depreciation) of futures contracts as reported in the Portfolio of Investments. The Statement of Assets and Liabilities only reflects the current day variation margin, receivable/payable to brokers.

The following tables set forth by primary risk exposure the Fund's realized gains (losses) and change in unrealized appreciation (depreciation) by type of derivative contract for the year ended December 31, 2009 in accordance with ASC 815.

Realized Gain (Loss)

Primary Risk Exposure	Derivative Type	Value (000)
Interest Rate Risk	Futures Contracts	\$(617)
Foreign Currency	Foreign Currency	
Contracts Risk	Exchange Contracts	123
Total		\$(494)

Change in Unrealized Appreciation (Depreciation)

Primary Risk Exposure	Derivative Type	Value (000)
Interest Rate Risk	Futures Contracts	\$709
Foreign Currency	Foreign Currency	
Contracts Risk	Exchange Contracts	85
Total		\$794

All open derivative positions at period end are reflected on the Fund's Portfolio of Investments and the volume of these open positions relative to the net assets of the Fund is generally representative of open positions throughout the reporting period.

5. Security Lending: At a meeting held on September 23-24, 2009, the Board of Directors authorized the Fund to lend securities to qualified financial institutions, such as broker-dealers, to earn additional income. As of December 31, 2009, there were no securities out on loan.

6. Micro-Finance Loans: A portion of the Fund's investments may include investments in microfinance loans. Microfinance loans are typically very small loans (microcredit) made for providing the means for people who are not served by traditional banking systems to expand their businesses or finance their families' basic needs by providing access to affordable credit. Microfinance loans carry many of the same risks associated with investing in

Morgan Stanley Emerging Markets Debt Fund, Inc.

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Notes to Financial Statements (cont d)

emerging markets countries, but because some of the microfinance loans may be used to fund crop growing and livestock, microfinance loans may also be subject to climate and geography risk. In addition, most micro-clients have low incomes and little or no previous credit history. As a result, there is no assurance that micro-clients will be able to repay the microfinance loans.

7. Fair Value Measurement: In accordance with FASB ASC 820 Fair Value Measurements and Disclosure (ASC 820) (formerly known as SFAS 157), fair value is defined as the price that the Fund would receive to sell an investment or pay to transfer a liability in a timely transaction with an independent buyer in the principal market, or in the absence of a principal market the most advantageous market for the investment or liability. ASC 820 establishes a three-tier hierarchy to distinguish between (1) inputs that reflect the assumptions market participants would use in valuing an asset or liability developed based on market data obtained from sources independent of the reporting entity (observable inputs) and (2) inputs that reflect the reporting entity's own assumptions about the assumptions market participants would use in valuing an asset or liability developed based on the best information available in the circumstances (unobservable inputs) and to establish classification of fair value measurements for disclosure purposes. Various inputs are used in determining the value of the Fund's investments. The inputs are summarized in the three broad levels listed below.

- Level 1 quoted prices in active markets for identical securities
- Level 2 other significant observable inputs (including quoted prices for similar investments, interest rates, prepayment speeds, credit risk, etc.)
- Level 3 significant unobservable inputs (including the Fund's own assumptions in determining the fair value of investments)

The inputs or methodology used for valuing securities are not necessarily an indication of the risk associated with investing in those securities.

8. Other: Security transactions are accounted for on the date the securities are purchased or sold. Realized gains (losses) on the sale of investment securities are determined on the specific identified cost basis. Interest income is recognized on the accrual basis and discounts and premiums on investments purchased are accreted or amortized in accordance with the effective yield method over their respective lives, except where collection is in doubt. Dividend income and distributions are recorded on the ex-dividend date (except certain dividends which may be

recorded as soon as the Fund is informed of such dividends) net of applicable withholding taxes.

B. Investment Advisory Fees: Morgan Stanley Investment Management Inc. (the Adviser or MS Investment Management) provides investment advisory services to the Fund under the terms of an Investment Advisory and Management Agreement (the Agreement). Under the Agreement, the Adviser is paid a fee computed weekly and payable monthly at an annual rate of 1.00% of the Fund s average weekly net assets.

C. Administration Fees: MS Investment Management also serves as Administrator to the Fund pursuant to an Administration Agreement. Under the Administration Agreement, the administration fee is 0.08% of the Fund s average weekly net assets. MS Investment Management has agreed to limit the administration fee through a waiver so that it will be no greater than the previous administration fee (prior to November 1, 2004) of 0.02435% of the Fund s average weekly net assets plus \$24,000 per annum. This waiver is voluntary and

Morgan Stanley Emerging Markets Debt Fund, Inc.

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Notes to Financial Statements (cont d)

may be terminated at any time. For the year ended December 31, 2009, approximately \$94,000 of administration fees were waived pursuant to this arrangement. Under a sub-administration agreement between the Administrator and JPMorgan Investor Services Co. (JPMIS), a corporate affiliate of JPMorgan Chase Bank, N.A., JPMIS provides certain administrative services to the Fund. For such services, the Administrator pays JPMIS a portion of the fee the Administrator receives from the Fund. Administration costs (including out-of-pocket expenses) incurred in the ordinary course of providing services under the Administration agreement, except pricing services and extraordinary expenses, are covered under the administration fee.

D. Custodian Fees: JPMorgan Chase Bank, N.A., (the Custodian) and its affiliates serve as Custodian for the Fund. The Custodian holds cash, securities, and other assets of the Fund as required by the 1940 Act. Custody fees are payable monthly based on assets held in custody, investment purchases and sales activity and account maintenance fees, plus reimbursement for certain out-of-pocket expenses.

The Fund has entered into an arrangement with its Custodian whereby credits realized on uninvested cash balances were used to offset a portion of the Fund's expenses. If applicable, these custodian credits are shown as Expense Offset in the Statement of Operations.

E. Federal Income Taxes: It is the Fund's intention to continue to qualify as a regulated investment company and distribute all of its taxable income. Accordingly, no provision for Federal income taxes is required in the financial statements. Distributions to stockholders are recorded on the ex-dividend date.

The Fund may be subject to taxes imposed by countries in which it invests. Such taxes are generally based on income and/ or capital gains earned or repatriated. Taxes are accrued and applied to net investment income, net realized gains and net unrealized appreciation as such income and/or gains are earned. FASB ASC 740-10 Income Taxes Overall (formerly known as FIN48) sets forth a minimum threshold for financial statement recognition of the benefit of a tax position taken or expected to be taken in a tax return. Management has concluded there are no significant uncertain tax positions that would require recognition in the financial statements. If applicable, the Fund recognizes interest accrued related to unrecognized tax benefits in Interest Expense and penalties in Other expenses on the Statement of Operations. The Fund files tax returns with the U.S. Internal Revenue Service, New York and various states. Generally, each of the tax years in the four year period ended December 31, 2009, remains subject to examination by taxing authorities.

The tax character of distributions paid may differ from the character of distributions shown on the Statements of Changes in Net Assets due to short-term capital gains being treated as ordinary income for tax purposes.

The tax character of distributions paid during fiscal 2009 and 2008 was as follows:

2009 Distributions Paid From: (000)		2008 Distributions Paid From: (000)	
Ordinary Income	Long-term Capital Gain	Ordinary Income	Long-term Capital Gain
\$13,364	\$	\$18,360	\$

The amount and character of income and capital gain distributions to be paid by the Fund are determined in accordance with Federal income tax regulations, which may differ from U.S. generally accepted accounting principles. The book/tax differences are considered either temporary or permanent in nature.

Temporary differences are generally due to differing book and tax treatments for the timing of the recognition of gains (losses)

Morgan Stanley Emerging Markets Debt Fund, Inc.

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Notes to Financial Statements (cont d)

on certain investment transactions and the timing of the deductibility of certain expenses.

Permanent differences, primarily due to differing treatments of gains (losses) related to foreign currency transactions, paydown adjustments, expiring capital losses, basis adjustments for securities sold and swap income adjustments, resulted in the following reclassifications among the components of net assets at December 31, 2009:

	Increase (Decrease)	
Undistributed (Distributions in Excess of) Net Investment Income (Loss) (000)	Accumulated Net Realized Gain (Loss) (000)	Paid-in Capital (000)
\$(3,455)	\$5,855	\$(2,400)

At December 31, 2009, the components of distributable earnings on a tax basis were as follows:

Undistributed Ordinary Income (000)	Undistributed Long-term Capital Gain (000)
\$110	\$

At December 31, 2009, the U.S. Federal income tax cost basis of investments was approximately \$248,434,000 and, accordingly, net unrealized appreciation for U.S. Federal income tax purposes was \$10,974,000 of which \$20,982,000 related to appreciated securities and \$10,008,000 related to depreciated securities.

At December 31, 2009, the Fund had a capital loss carryforward for U.S. Federal income tax purposes of approximately \$5,202,000 to offset against future capital gains which will expire on December 31, 2016.

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During the year ended December 31, 2009, the Fund had utilized and expired capital loss carryforward for U.S. Federal income tax purposes of approximately \$1,058,000 and \$2,400,000, respectively.

To the extent that capital loss carryforwards are used to offset any future capital gains realized during the carryover period as provided by U.S. Federal income tax regulations, no capital gains tax liability will be incurred by the Fund for gains realized and not distributed. To the extent that capital gains are offset, such gains will not be distributed to the stockholders.

F. Contractual Obligations: The Fund enters into contracts that contain a variety of indemnifications. The Fund's maximum exposure under these arrangements is unknown. However, the Fund has not had prior claims or losses pursuant to these contracts and expects the risk of loss to be remote.

G. Security Transactions and Transactions with Affiliates: The Fund invests in the Institutional Class of the Morgan Stanley Institutional Liquidity Funds Money Market Portfolio (the Liquidity Funds), an open-end management investment company managed by the Adviser. Investment Advisory fees paid by the Fund are reduced by an amount equal to its pro-rata share of advisory and administration fees paid by the Fund due to its investment in the Liquidity Funds. For the year ended December 31, 2009, advisory fees paid were reduced by approximately \$4,000 relating to the Fund's investment in the Liquidity Funds.

A summary of the Fund's transactions in shares of the Liquidity Funds during the year ended December 31, 2009 is as follows:

Market Value December 31, 2008 (000)	Purchases at Cost (000)	Sales Proceeds (000)	Dividend Income (000)	Market Value December 31, 2009 (000)
\$7,662	\$125,609	\$129,780	\$8	\$3,491

During the year ended December 31, 2009, the Fund made purchases and sales totaling approximately \$198,281,000 and \$188,359,000, respectively, of investment securities other than long-term U.S. Government securities and short-term investments. There were no purchases or sales of long-term U.S. Government securities.

Morgan Stanley Emerging Markets Debt Fund, Inc.

December 31, 2009

Notes to Financial Statements (cont d)

These investments may be traded by one market maker who may also be utilized by the Fund to provide pricing information used to value such securities. The amounts which will be realized upon disposition of the securities may differ from the value reflected on the Statement of Assets and Liabilities and the differences could be material.

During the year ended December 31, 2009, the Fund incurred no brokerage commissions with Morgan Stanley & Co. Incorporated, an affiliated broker/dealer.