

Morgan Stanley Emerging Markets Domestic Debt Fund, Inc.  
Form N-CSR  
January 09, 2013

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 811-022011

Morgan Stanley Emerging Markets Domestic Debt  
(Exact name of registrant as specified in charter)

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

10036  
(Zip code)

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

Registrant's telephone number, including area code: 201-830-8894

Date of fiscal year end: October 31, 2012

Date of reporting period: October 31, 2012

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Item 1 - Report to Shareholders

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**Morgan Stanley Emerging Markets Domestic Debt Fund, Inc.**

**Directors**

Frank L. Bowman

Michael Bozic

Kathleen A. Dennis

James F. Higgins

Dr. Manuel H. Johnson

Joseph J. Kearns

Michael F. Klein

Michael E. Nugent

W. Allen Reed

Fergus Reid

**Officers**

Michael E. Nugent

*Chairperson of the Board*

Arthur Lev

*President and Principal Executive Officer*

Mary Ann Picciotto

*Chief Compliance Officer*

Stefanie V. Chang Yu

*Vice President*

Francis J. Smith

*Treasurer and Principal Financial Officer*

Mary E. Mullin

*Secretary*

**Adviser and Administrator**

Morgan Stanley Investment Management Inc.

522 Fifth Avenue

New York, New York 10036

**Custodian**

State Street Bank and Trust Company

One Lincoln Street

Boston, Massachusetts 02111

**Stockholder Servicing Agent**

Computershare Trust Company, N.A.

250 Royall Street

Canton, Massachusetts 02021

**Legal Counsel**

Dechert LLP

1095 Avenue of the Americas

New York, New York 10036

**Independent Registered Public Accounting Firm**

Ernst & Young LLP

200 Clarendon Street

Boston, Massachusetts 02116

For additional Fund information, including the Fund's net asset value per share and information regarding the investments comprising the Fund's portfolio, please call toll free 1 (800) 231-2608 or visit our website at [www.morganstanley.com/im](http://www.morganstanley.com/im). All investments involve risks, including the possible loss of principal.

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INVESTMENT MANAGEMENT

Morgan Stanley

Emerging Markets Domestic

Debt Fund, Inc.

NYSE: EDD

**Morgan Stanley**

**Investment Management Inc.**

**Adviser**

**Annual Report**

**October 31, 2012**

CEEDDANN

IU12-02571P-Y10/12

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**Morgan Stanley Emerging Markets Domestic Debt Fund, Inc.**

**October 31, 2012**

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## **Morgan Stanley Emerging Markets Domestic Debt Fund, Inc.**

**October 31, 2012**

Letter to Stockholders (unaudited)

### **Performance**

For the year ended October 31, 2012, the Morgan Stanley Emerging Markets Domestic Debt Fund, Inc. (the "Fund") had total returns of 9.61%, based on net asset value, and 11.38% based on market value per share (including reinvestment of distributions), compared to its benchmark, the J.P. Morgan Government Bond Index-Emerging Markets Global Diversified Index (the "Index")\*, which returned 7.25%. On October 31, 2012, the closing price of the Fund's shares on the New York Stock Exchange was \$16.47, representing a 7.0% discount to the Fund's net asset value per share. Past performance is no guarantee of future results.

### **Factors Affecting Performance**

- In the fourth quarter of 2011 and into the first two months of 2012, global risk assets strengthened on positive signs of recovery out of the U.S. and improved sentiment toward steps taken by European policymakers to put Europe on the path to resolving its credit crisis.
- However, from March through May, U.S. economic optimism could not overcome fears about global growth due to Greek political and debt-sustainability concerns, signs of distress out of the Euro area periphery, U.S. Treasury yields at record lows, and softer Chinese economic data. In addition, the U.S. labor market saw little progress.
- Global risk assets recovered partially in June as risk sentiment modestly improved. Moreover, in the 3rd quarter of 2012, investor sentiment greatly improved as decisive policy measures in developed markets helped reduce tail risks for investors, particularly in the Euro area, and fostered a more supportive macro environment.
- Emerging market (EM) currencies were mixed over the period as global concerns weighed on investors. Among developed markets, the euro declined sharply against the U.S. dollar as worries about the euro-zone debt crisis and Europe's sluggish economy overshadowed European policymakers' efforts.
- Dedicated-emerging markets debt funds saw inflows of \$31.3 billion for the one-year period as of the end of October 31, 2012, according to data from EmergingPortfolio (EPFR Global). After strong demand for local currency EM funds for most of 2011, a loss of 11.6% in EM currencies triggered in September 2011 led to large outflows from local currency funds. Inflows subsequently shifted into the more defensive hard currency EM debt funds that invest in bonds denominated in U.S. dollars and other developed market currencies. These hard currency funds attracted inflows of \$20.8 billion, while local currency funds experienced inflows of \$6.2 billion and blended currency funds gained a more modest \$4.3 billion in assets.
- The portfolio benefited from overweight exposure to Colombia, Mexico, Poland, South Africa, and Turkey, as well as an out of benchmark position in Venezuelan external debt. Colombia benefited from robust domestic demand, strong foreign investment into its oil and mining sectors, and reduced security concerns about FARC guerillas. Mexico advanced due to resilient economic activity despite downside risks of a sharp moderation in the U.S., Mexico's largest export market. With a weakening Europe and its own growth trending lower, Poland benefited from euro-zone optimism and relative resilience to negative regional developments. Euro-zone optimism also aided South Africa due to its close financial and trade linkages with Europe, despite significant political and mining labor tensions. Turkey outperformed as European Central Bank (ECB) and Federal Reserve (Fed) bond purchases buoyed demand for higher-yielding assets. Risk remained, however, as economic activity has slowed and cross-border fire from Syria has

intensified. Venezuela benefited from high oil prices and reports about market-unfriendly President Hugo Chavez's failing health and inability to win October's presidential election.

## **Morgan Stanley Emerging Markets Domestic Debt Fund, Inc.**

**October 31, 2012**

Letter to Stockholders (unaudited) (cont'd)

- Conversely, overweight exposure to Brazilian currency as well as underweight exposure to Indonesia, Malaysia and Russia detracted from relative returns. Brazil underperformed due to worries that its central bank would take measures to manage the Brazilian currency's value in the market, likely limiting currency appreciation. Indonesia outperformed due to strong growth and domestic demand, despite persistent concerns about Indonesia's weaker export sector due to a deterioration in external demand, while Malaysia benefited from robust domestic demand, moderating gasoline prices and diminished inflation concerns. Russia outperformed due to high oil prices, strong private consumption, and political stability.

### **Management Strategies**

- We expect the global economy to exhibit varying degrees of economic recovery for the remainder of 2012, as developed market growth will likely remain well below potential, with emerging economies growing at a healthier pace. We believe that this growth differential will remain throughout 2012 and well into 2013. However, global growth has moderated, as the trade linkage between developed and emerging markets has been a constraint on growth in the latter. We anticipate that emerging markets will from time to time come under pressure until there is some resolution to fiscal issues in Europe and growth in the U.S. regains its footing.
- The Fed, ECB and Bank of Japan (BOJ) have committed to policy easing, which has helped support commodity prices and capital inflows into emerging countries, and bolstered demand for higher-yielding assets. The impact of ongoing liquidity-providing operations will likely offset the negative effect of global headwinds somewhat, in our view. However, we believe that market direction continues to closely mirror the ongoing issues in Europe and the pace of economic activity in the U.S. and China.
- Despite challenges that lay ahead, we remain positive on emerging markets debt prospects. There has been a shift thus far this year toward more of an easing bias among emerging economies, however, recent food and energy inflation pressures suggest that policy easing in EM may be put on hold. We believe that EM central banks will continue to adopt policies aimed at limiting local currency appreciation this year, but will not be able to reverse the longer-term appreciation trend in their currencies.

Sincerely,

Arthur Lev  
President and Principal Executive Officer November 2012

\* J.P. Morgan Government Bond Index Emerging Markets Global Diversified Index tracks local currency government bonds issued by emerging markets. It is not possible to invest directly in an Index.

## **Morgan Stanley Emerging Markets Domestic Debt Fund, Inc.**

**October 31, 2012**

Investment Advisory Agreement Approval (unaudited)

### **Nature, Extent and Quality of Services**

The Board reviewed and considered the nature and extent of the investment advisory services provided by the Adviser (as defined herein) under the advisory agreement, including portfolio management, investment research and equity and fixed income securities trading. The Board also reviewed and considered the nature and extent of the non-advisory, administrative services provided by the Fund's Adviser under the administration agreement, including accounting, clerical, bookkeeping, compliance, business management and planning, and the provision of supplies, office space and utilities at the Adviser's expense. (The advisory and administration agreements together are referred to as the "Management Agreement.") The Board also compared the nature of the services provided by the Adviser with similar services provided by non-affiliated advisers as reported to the Board by Lipper, Inc. ("Lipper").

The Board reviewed and considered the qualifications of the portfolio managers, the senior administrative managers and other key personnel of the Adviser who provide the advisory and administrative services to the Fund. The Board determined that the Adviser's portfolio managers and key personnel are well qualified by education and/or training and experience to perform the services in an efficient and professional manner. The Board concluded that the nature and extent of the advisory and administrative services provided were necessary and appropriate for the conduct of the business and investment activities of the Fund and supported its decision to approve the Management Agreement.

### **Performance, Fees and Expenses of the Fund**

The Board reviewed the performance, fees and expenses of the Fund compared to its peers, as determined by Lipper, and to appropriate benchmarks where applicable. The Board discussed with the Adviser the performance goals and the actual results achieved in managing the Fund. When considering a fund's performance, the Board and the Adviser place emphasis on trends and longer-term returns (focusing on one-year, three-year and five-year performance as of December 31, 2011, or since inception, as applicable). When a fund underperforms its benchmark and/or its peer group average, the Board and the Adviser discuss the causes of such underperformance and, where necessary, they discuss specific changes to investment strategy or investment personnel. The Board noted that the Fund's performance was below its peer group average for the one- and three-year periods but better than its peer group average since the end of April 2007, the month of the Fund's inception. The Board discussed with the Adviser the level of the advisory and administration fees (together, the "management fee") for this Fund relative to comparable funds and/or other accounts advised by the Adviser and/or compared to its peers as determined by Lipper. In addition to the management fee, the Board also reviewed the Fund's total expense ratio. The Board noted that the Fund's management fee was higher than its peer group average and the total expense ratio was higher but close to its peer group average. After discussion, the Board concluded that: (i) the Fund's performance was acceptable; (ii) the Fund's management fee was acceptable given the quality and nature of services provided; and (iii) the Fund's total expense ratio was competitive with its peer group average.

### **Economies of Scale**

The Board considered the size and growth prospects of the Fund and how that relates to the Fund's total expense ratio and particularly the Fund's management fee rate, which does not include breakpoints. In conjunction with its review of the Adviser's profitability, the Board discussed with the Adviser how a change in assets can affect the efficiency or effectiveness of managing the Fund and whether



## **Morgan Stanley Emerging Markets Domestic Debt Fund, Inc.**

**October 31, 2012**

### **Investment Advisory Agreement Approval (unaudited) (cont'd)**

the management fee level is appropriate relative to current and projected asset levels and/or whether the management fee structure reflects economies of scale as asset levels change. The Board considered that, with respect to closed-end funds, the assets are not likely to grow with new sales or grow significantly as a result of capital appreciation. The Board concluded that economies of scale for the Fund were not a factor that needed to be considered at the present time.

### **Profitability of the Adviser and Affiliates**

The Board considered information concerning the costs incurred and profits realized by the Adviser and its affiliates during the last year from their relationship with the Fund and during the last two years from their relationship with the Morgan Stanley Fund Complex and reviewed with the Adviser the cost allocation methodology used to determine the profitability of the Adviser and affiliates. The Board has determined that its review of the analysis of the Adviser's expenses and profitability supports its decision to approve the Management Agreement.

### **Other Benefits of the Relationship**

The Board considered other benefits to the Adviser and its affiliates derived from their relationship with the Fund and other funds advised by the Adviser. These benefits may include, among other things, "float" benefits derived from handling of checks for purchases and sales, research received by the Adviser generated from commission dollars spent on funds' portfolio trading and fees for distribution and/or shareholder servicing. The Board reviewed with the Adviser each of these arrangements and the reasonableness of the Adviser's costs relative to the services performed. The Board has determined that its review of the other benefits received by the Adviser or its affiliates supports its decision to approve the Management Agreement.

### **Resources of the Adviser and Historical Relationship Between the Fund and the Adviser**

The Board considered whether the Adviser is financially sound and has the resources necessary to perform its obligations under the Management Agreement. The Board also reviewed and considered the historical relationship between the Fund and the Adviser, including the organizational structure of the Adviser, the policies and procedures formulated and adopted by the Adviser for managing the Fund's operations and the Board's confidence in the competence and integrity of the senior managers and key personnel of the Adviser. The Board concluded that the Adviser has the financial resources necessary to fulfill its obligations under the Management Agreement and that it is beneficial for the Fund to continue its relationship with the Adviser.

### **Other Factors and Current Trends**

The Board considered the controls and procedures adopted and implemented by the Adviser and monitored by the Fund's Chief Compliance Officer and concluded that the conduct of business by the Adviser indicates a good faith effort on its part to adhere to high ethical standards in the conduct of the Fund's business.

### **General Conclusion**

After considering and weighing all of the above factors, the Board concluded that it would be in the best interest of the Fund and its shareholders to approve renewal of the Management Agreement for another year. In reaching this

conclusion the Board did not give particular weight to any single factor referenced above. The Board considered these factors over the course of numerous meetings,

**Morgan Stanley Emerging Markets Domestic Debt Fund, Inc.**

**October 31, 2012**

Investment Advisory Agreement Approval (unaudited) (cont'd)

some of which were in executive session with only the independent Board members and their counsel present. It is possible that individual Board members may have weighed these factors differently in reaching their individual decisions to approve the Management Agreement.





**Morgan Stanley Emerging Markets Domestic Debt Fund, Inc.****October 31, 2012**

Portfolio of Investments

*(Showing Percentage of Total Value of Investments)*

	<b>Face Amount (000)</b>	<b>Value (000)</b>
<b>FIXED INCOME SECURITIES (98.9%)</b>		
<b>Argentina (3.0%)</b>		
<b>Sovereign (3.0%)</b>		
Argentina Boden Bonds, 7.00%, 10/3/15	\$ 58,500	\$ 48,394
<b>Brazil (16.2%)</b>		
<b>Sovereign (16.2%)</b>		
Brazil Notas do Tesouro Nacional, Series F, 10.00%, 1/1/14	BRL 522,640	264,621
<b>Chile (0.6%)</b>		
<b>Sovereign (0.6%)</b>		
Chile Government International Bond, 5.50%, 8/5/20	CLP 4,665,000	10,588
<b>Colombia (4.1%)</b>		
<b>Sovereign (4.1%)</b>		
Colombia Government International Bond, 7.75%, 4/14/21	COP 29,000,000	20,066
9.85%, 6/28/27	46,000,000	39,301
12.00%, 10/22/15	11,000,000	7,445
		66,812
<b>Hungary (6.9%)</b>		
<b>Sovereign (6.9%)</b>		
Hungary Government Bond, 6.75%, 2/24/17	HUF 8,488,920	39,415
7.50%, 11/12/20	15,180,000	72,705
		112,120
<b>Indonesia (6.9%)</b>		
<b>Sovereign (6.9%)</b>		
Barclays Bank PLC, Indonesia Government Bonds, Credit Linked Notes, 10.00%, 7/17/17 (a)(b)	IDR360,000,000	44,653
Credit Suisse, Indonesia Government Bonds, Credit Linked Notes,	154,683,530	19,186

10.00%, 7/17/17		
Deutsche Bank AG, Republic of Indonesia Government Bond, Credit Linked Notes, 11.00%, 12/15/20 (a)(b)	60,000,000	8,383
	<b>Face Amount (000)</b>	<b>Value (000)</b>

JPMorgan Chase Bank, London, Indonesia Government Bonds, Credit Linked Notes, 8.25%, 7/17/21	IDR 135,000,000	\$ 16,520
10.00%, 7/19/17 (b)	192,525,000	23,880
		112,622

**Malaysia (3.1%)****Sovereign (3.1%)**

Malaysia Government Bond, 3.84%, 8/12/15	MYR 110,000	36,873
5.09%, 4/30/14	42,152	14,252
		51,125

**Mexico (15.5%)****Sovereign (15.5%)**

Mexican Bonos, 8.00%, 6/11/20	MXN 2,104,027	187,015
Petroleos Mexicanos (Units), 7.65%, 11/24/21 (a)(c)	791,300	66,215
		253,230

**Peru (2.0%)****Sovereign (2.0%)**

Peru Government Bond, 7.84%, 8/12/20	PEN 37,745	18,060
Peruvian Government International Bond (Units), 7.84%, 8/12/20 (c)	30,000	14,355
		32,415

**Philippines (1.0%)****Sovereign (1.0%)**

Philippine Government International Bond, 4.95%, 1/15/21	PHP 648,000	17,342
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**Poland (8.8%)****Sovereign (8.8%)**

Poland Government Bond, 5.25%, 10/25/20	PLN 314,000	103,859
5.50%, 10/25/19	117,287	39,460
		143,319

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



**Morgan Stanley Emerging Markets Domestic Debt Fund, Inc.****October 31, 2012**

Portfolio of Investments (cont'd)

*(Showing Percentage of Total Value of Investments)*

	Face Amount (000)	Value (000)
<b>Russia (2.9%)</b>		
<b>Sovereign (2.9%)</b>		
Russian Foreign Bond		
Eurobond,		
7.85%, 3/10/18 (a)	RUB 1,095,000	\$ 37,468
7.85%, 3/10/18	290,000	9,923
		47,391
<b>South Africa (9.0%)</b>		
<b>Sovereign (9.0%)</b>		
South Africa		
Government Bond,		
6.75%, 3/31/21	ZAR 779,000	90,400
7.25%, 1/15/20	465,411	56,097
		146,497
<b>Thailand (4.0%)</b>		
<b>Sovereign (4.0%)</b>		
Thailand Government Bond,		
4.25%, 3/13/13	THB 1,597,940	52,397
5.25%, 7/13/13	395,100	13,105
		65,502
<b>Turkey (11.0%)</b>		
<b>Sovereign (11.0%)</b>		
Turkey Government Bond,		
10.50%, 1/15/20	TRY 278,825	179,117
<b>Venezuela (3.9%)</b>		
<b>Sovereign (3.9%)</b>		
Petroleos de Venezuela SA,		
8.50%, 11/2/17	\$ 69,000	62,100
Venezuela Government		
International Bond,		
9.25%, 9/15/27	1,349	1,224
		63,324
<b>TOTAL FIXED INCOME</b>		
<b>SECURITIES</b>		
(Cost \$1,628,820)		1,614,419
	<b>Shares</b>	<b>Value (000)</b>
<b>SHORT-TERM INVESTMENT (1.1%)</b>		

**Investment Company (1.1%)**

Morgan Stanley Institutional Liquidity Funds Money Market Portfolio Institutional Class (See Note F) (Cost \$18,635)	18,634,580	\$ 18,635
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**TOTAL INVESTMENTS****(100.0%)**(Cost \$1,647,455) (d) 1,633,054**LIABILITIES IN EXCESS OF  
OTHER ASSETS**(349,953)**NET ASSETS**\$1,283,101

(a) 144A security Certain conditions for public sale may exist. Unless otherwise noted, these securities are deemed to be liquid.

(b) 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 October 31, 2012.

(c) Consists of one or more classes of securities traded together as a unit.

(d) Securities are available for collateral in connection with open foreign currency exchange contracts.

**Foreign Currency Exchange Contracts Information:**

The Fund had the following foreign currency exchange contracts open at October 31, 2012:

Counterparty	Currency to Deliver (000)	Value (000)	Settlement Date	In Exchange For (000)	Value (000)	Unrealized Appreciation (Depreciation) (000)	
JPMorgan Chase Bank	USD	79,348	\$ 79,348	11/19/12 RUB	2,475,347	\$ 78,692	\$ (656)
JPMorgan Chase Bank	USD	72,206	72,206	11/29/12 MYR	221,930	72,710	504
JPMorgan Chase Bank	USD	22,015	22,015	11/30/12 THB	678,000	22,081	66
			\$173,569			\$173,483	\$ (86)

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

**Morgan Stanley Emerging Markets Domestic Debt Fund, Inc.**

**October 31, 2012**

Portfolio of Investments (cont'd)

BRL	Brazilian Real
CLP	Chilean Peso
COP	Colombian Peso
HUF	Hungarian Forint
IDR	Indonesian Rupiah
MXN	Mexican New Peso
MYR	Malaysian Ringgit
PEN	Peruvian Nuevo Sol
PHP	Philippine Peso
PLN	Polish Zloty
RUB	Russian Ruble
THB	Thai Baht
TRY	Turkish Lira
USD	United States Dollar
ZAR	South African Rand

**Portfolio Composition**

<b>Classification</b>	<b>Percentage of Total Investments</b>
Sovereign	98.9%
Other*	1.1
<b>Total Investments</b>	<b>100.0%**</b>

\* Industries and/or investment types representing less than 5% of total investments.

\*\* Does not include open forward foreign currency contracts with net unrealized depreciation of approximately \$86,000.

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







**Morgan Stanley Emerging Markets Domestic Debt Fund, Inc.****October 31, 2012**

Financial Statements

	<b>October 31, 2012</b>
	<b>(000)</b>
<b>Statement of Assets and Liabilities</b>	
<b>Assets:</b>	
Investments in Securities of Unaffiliated Issuers, at Value (Cost \$1,628,820)	\$ 1,614,419
Investment in Security of Affiliated Issuer, at Value (Cost \$18,635)	18,635
Total Investments in Securities, at Value (Cost \$1,647,455)	1,633,054
Foreign Currency, at Value (Cost \$8,971)	9,018
Interest Receivable	37,960
Receivable for Lehman Brothers Closed Reverse Repurchase Transactions	4,389
Unrealized Appreciation on Foreign Currency Exchange Contracts	570
Receivable from Affiliate	3
Other Assets	568
<b>Total Assets</b>	<b>1,685,562</b>
<b>Liabilities:</b>	
Payable for Line of Credit	400,019
Payable for Advisory Fees	1,428
Unrealized Depreciation on Foreign Currency Exchange Contracts	656
Payable for Custodian Fees	129
Payable for Administration Fees	114
Payable for Professional Fees	52
Payable for Stockholder Servicing Agent Fees	1
Other Liabilities	62
<b>Total Liabilities</b>	<b>402,461</b>
<b>Net Assets</b>	
Applicable to 72,431,536 Issued and Outstanding \$0.01 Par Value Shares (100,000,000 Shares Authorized)	\$ 1,283,101
<b>Net Asset Value Per Share</b>	<b>\$ 17.71</b>
<b>Net Assets Consist of:</b>	
Common Stock	\$ 724
Paid-in-Capital	1,303,597
Accumulated Undistributed Net Investment Income	12,245
Accumulated Net Realized Loss	(19,182)
Unrealized Appreciation (Depreciation) on:	
Investments	(14,401)
Foreign Currency Exchange Contracts	(86)
Foreign Currency Translations	204
<b>Net Assets</b>	<b>\$ 1,283,101</b>

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



**Morgan Stanley Emerging Markets Domestic Debt Fund, Inc.****October 31, 2012**

Financial Statements (cont'd)

	<b>Year Ended October 31, 2012 (000)</b>
Statement of Operations	
<b>Investment Income:</b>	
Interest from Securities of Unaffiliated Issuers	\$ 122,189
Dividends from Security of Affiliated Issuer	25
<b>Total Investment Income</b>	122,214
<b>Expenses:</b>	
Advisory Fees (Note B)	16,444
Administration Fees (Note C)	1,316
Administrative Fees on Line of Credit (Note G)	860
Custodian Fees (Note D)	826
Stockholder Reporting Expenses	167
Professional Fees	138
Directors' Fees and Expenses	35
Commitment Fee (Note G)	7
Stockholder Servicing Agent Fees	7
Other Expenses	76
<b>Expenses Before Non Operating Expenses</b>	19,876
Interest Expense on Line of Credit (Note G)	7,061
<b>Total Expenses</b>	26,937
Rebate from Morgan Stanley Affiliate (Note F)	(22)
Expense Offset (Note D)	( @)
<b>Net Expenses</b>	26,915
<b>Net Investment Income</b>	95,299
<b>Realized Gain (Loss):</b>	
Investments Sold	12,609
Foreign Currency Exchange Contracts	5,376
Foreign Currency Transactions	(8,760)
<b>Net Realized Gain</b>	9,225
<b>Change in Unrealized Appreciation (Depreciation):</b>	
Investments	7,972
Foreign Currency Exchange Contracts	(3,602)
Foreign Currency Translations	1,885
<b>Net Change in Unrealized Appreciation (Depreciation)</b>	6,255
<b>Net Realized Gain and Change in Unrealized Appreciation (Depreciation)</b>	15,480
<b>Net Increase in Net Assets Resulting from Operations</b>	\$ 110,779

@ Amount is less than \$500.

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



**Morgan Stanley Emerging Markets Domestic Debt Fund, Inc.****October 31, 2012**

Financial Statements (cont'd)

	<b>Year Ended October 31, 2012 (000)</b>	<b>Year Ended October 31, 2011 (000)</b>
Statements of Changes in Net Assets		
<b>Increase (Decrease) in Net Assets</b>		
Operations:		
Net Investment Income	\$ 95,299	\$ 110,074
Net Realized Gain	9,225	29,356
Net Change in Unrealized Appreciation (Depreciation)	6,255	(142,563)
<b>Net Increase (Decrease) in Net Assets Resulting from Operations</b>	<b>110,779</b>	<b>(3,133)</b>
Distributions from and/or in Excess of:		
Net Investment Income	(83,296)	(86,918)
<b>Total Increase (Decrease)</b>	<b>27,483</b>	<b>(90,051)</b>
<b>Net Assets:</b>		
Beginning of Period	1,255,618	1,345,669
<b>End of Period (Including Accumulated Undistributed Net Investment Income of \$12,245 and \$16,413)</b>	<b>\$1,283,101</b>	<b>\$1,255,618</b>

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

**Morgan Stanley Emerging Markets Domestic Debt Fund, Inc.****October 31, 2012**

Financial Statements (cont'd)

	<b>Year Ended October 31, 2012 (000)</b>
Statement of Cash Flows	
<b>Cash Flows From Operating Activities:</b>	
Proceeds from Sales and Maturities of Long-Term Investments	\$ 1,018,874
Purchase of Long-Term Investments	(1,057,047)
Net (Increase) Decrease in Short-Term Investments	(14,812)
Net (Increase) Decrease in Foreign Currency Holdings	(3,278)
Net Realized Gain (Loss) for Foreign Currency Transactions and Exchange Contracts	(3,384)
Net Investment Income	95,299
<b>Adjustments to Reconcile Net Investment Income to Net Cash Provided (Used) by Operating Activities:</b>	
Net (Increase) Decrease in Receivables Related to Operations	1,909
Net (Increase) Decrease in Payables Related to Operations	77
Accretion/Amortization of Discounts and Premiums	(2,342)
Net Cash Provided for (Used by) Operating Activities	35,296
<b>Cash Flows From Financing Activities:</b>	
Cash Received for Line of Credit	48,000
Cash Distribution Paid	(83,296)
Net Cash Provided for (Used by) Financing Activities	(35,296)
Net Increase (Decrease) in Cash	
<b>Cash at Beginning of Period</b>	
<b>Cash at End of Period</b>	<b>\$</b>
<b>Supplemental Disclosure of Cash Flow Information:</b>	
Interest Paid on Line of Credit during the Period	\$ 7,067

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

**Morgan Stanley Emerging Markets Domestic Debt Fund, Inc.****October 31, 2012**

Financial Highlights

**Selected Per Share Data and Ratios**

	Year Ended October 31,				
	2012	2011	2010	2009	2008
<b>Net Asset Value, Beginning of Period</b>	\$ 17.34	\$ 18.58	\$ 16.17	\$ 12.61	\$ 20.47
Net Investment Income†	1.32	1.52	1.46	1.37	2.12
Net Realized and Unrealized Gain (Loss)	0.20	(1.56)	2.15	3.40	(7.49)
Total from Investment Operations	1.52	(0.04)	3.61	4.77	(5.37)
Distributions from and/or in excess of:					
Net Investment Income	(1.15)	(1.20)	(1.20)	(0.50)	(2.40)
Net Realized Gain					(0.09)
Return of Capital				(0.75)	
Total Distributions	(1.15)	(1.20)	(1.20)	(1.25)	(2.49)
Anti-Dilutive Effect of Share Repurchase Program				0.04	(0.00)‡
<b>Net Asset Value, End of Period</b>	\$ 17.71	\$ 17.34	\$ 18.58	\$ 16.17	\$ 12.61
<b>Per Share Market Value, End of</b>	\$ 16.47	\$ 15.87	\$ 17.29	\$ 13.75	\$ 9.70



**Period****TOTAL INVESTMENT RETURN:**

Market Value	11.38%	(1.34)%	35.60%	57.23%	(39.43)%
Net Asset Value(1)	9.61%	0.32%	23.83%	42.32%	(27.22)%

**RATIOS, SUPPLEMENTAL DATA:**

<b>Net Assets, End of Period (Thousands)</b>	\$1,283,101	\$1,255,618	\$1,345,669	\$1,171,520	\$923,962
Ratio of Expenses to Average Net Assets	2.16%+	2.07%+	2.28%+	2.20%+	2.80%+
Ratio of Expenses to Average Net Assets Excluding Non Operating Expenses	1.59%+	1.55%+	1.62%+	1.58%+	1.59%+
Ratio of Net Investment Income to Average Net Assets	7.63%+	8.36%+	8.61%+	9.60%+	11.90%+
Ratio of Rebate from Morgan Stanley Affiliates to Average Net Assets	0.00%§	0.00%§	0.00%§	0.00%§	0.00%§
Portfolio Turnover Rate	64%	100%	42%	74%	130%

(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.

† Per share amount is based on average shares outstanding.

‡ Amount is less than \$0.005 per share.

+ 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."

§ Amount is less than 0.005%.

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



## Morgan Stanley Emerging Markets Domestic Debt Fund, Inc.

October 31, 2012

### Notes to Financial Statements

The Morgan Stanley Emerging Markets Domestic Debt Fund, Inc. (the "Fund") was incorporated in Maryland on January 25, 2007 and is registered as a non-diversified, closed-end management investment company under the Investment Company Act of 1940, as amended (the "Act"). The Fund's primary investment objective is to seek a high level of current income, with a secondary investment objective of long-term capital appreciation. The Fund seeks to achieve its investment objectives by investing, under normal circumstances, at least 80% of its managed assets in emerging markets domestic debt. To the extent the Fund invests in derivative instruments, Morgan Stanley Investment Management Inc. (the "Adviser"), believes have economic characteristics similar to such securities, such investments will be counted for purposes of the Fund's policy described in the previous sentence. To the extent the Fund makes such investments, the Fund will be subject to the risk 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 ("GAAP"). Such policies are consistently followed by the Fund in the preparation of its financial statements. GAAP 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, except as noted

below. 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 last reported bid and ask prices. 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. Short-term debt securities purchased with remaining maturities of 60 days or less are valued at amortized cost, unless the Fund's Board of Directors (the "Directors") determines such valuation does not reflect the securities' fair value, in which case these securities will be valued at their fair value as determined in good faith under procedures adopted by the Directors.

Under procedures approved by the Directors, the Fund's Adviser has formed a Valuation Committee. The Valuation Committee provides administration and oversight of the Fund's valuation policies and procedures, which are reviewed at least annually by the Directors. Among other things, these procedures allow the Fund to utilize independent pricing services, quotations from securities and financial instrument dealers, and other market sources to determine fair value.

The Fund has procedures to determine the fair value of securities and other financial instruments for which market prices are not readily available. Under these procedures, the Valuation Committee convenes on a regular and ad hoc basis to review such securities and considers a number of factors, including valuation methodologies and significant unobservable valuation inputs, when arriving at fair value. The Valuation Committee may employ a market-based approach which may use related or comparable assets or liabilities, recent transactions, market multiples, book values, and other relevant information for the investment to determine the fair value of the investment. An



## Morgan Stanley Emerging Markets Domestic Debt Fund, Inc.

October 31, 2012

### Notes to Financial Statements (cont'd)

income-based valuation approach may also be used in which the anticipated future cash flows of the investment are discounted to calculate fair value. Discounts may also be applied due to the nature or duration of any restrictions on the disposition of the investments. Due to the inherent uncertainty of valuations of such investments, the fair values may differ significantly from the values that would have been used had an active market existed. The Valuation Committee employs various methods for calibrating these valuation approaches including a regular review of valuation methodologies, key inputs and assumptions, transactional back-testing or disposition analysis, and reviews of any related market activity.

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 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. Fair Value Measurement:** Financial Accounting Standards Board ("FASB") Accounting Standards Codification™ ("ASC") 820, "Fair Value Measurements and Disclosures" ("ASC 820"), defines fair value as the value 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 unadjusted quoted prices in active markets for identical investments
- 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. 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

The inputs or methodology used for valuing securities are not necessarily an indication of the risk associated with investing in those securities and the determination of the significance of a particular input to the fair value measurement in its entirety requires judgment and considers factors specific to each security.



**Morgan Stanley Emerging Markets Domestic Debt Fund, Inc.****October 31, 2012**

Notes to Financial Statements (cont'd)

The following is a summary of the inputs used to value the Fund's investments as of October 31, 2012.

**Fair Value Measurement Information:**

<b>Investment Type</b>	<b>Level 1 Unadjusted quoted prices (000)</b>	<b>Level 2 Other significant observable inputs (000)</b>	<b>Level 3 Significant unobservable inputs (000)</b>	<b>Total (000)</b>
<b>Assets:</b>				
<b>Fixed Income Securities</b>				
<b>Sovereign</b>	\$	\$1,614,419	\$	\$1,614,419
<b>Short-Term Investment</b>				
<b>Investment Company</b>	18,635			18,635
<b>Foreign Currency Exchange Contracts</b>				
<b>Total</b>		570		570
<b>Assets</b>	<b>18,635</b>	<b>1,614,989</b>		<b>1,633,624</b>
<b>Liabilities:</b>				
<b>Foreign Currency Exchange Contracts</b>				
<b>Total</b>		(656)		(656)
<b>Liabilities</b>		<b>(656)</b>		<b>(656)</b>
<b>Total</b>	<b>\$ 18,635</b>	<b>\$1,614,333</b>	<b>\$</b>	<b>\$1,632,968</b>

Transfers between investment levels may occur as the markets fluctuate and/or the availability of data used in an investment's valuation changes. The Fund recognizes transfers between the levels as of the end of the period. As of October 31, 2012, the Fund did not have any investments transfer between investment levels.

**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 ask prices of such currencies against U.S. dollars last quoted by a major bank as follows:

investments, other assets and liabilities at the prevailing rate 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 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. However, pursuant to U.S. Federal income tax regulations, gains and losses from certain foreign currency transactions and the foreign currency portion of gains and losses realized on sales and maturities of foreign denominated debt securities are treated as ordinary income for U.S. Federal income tax purposes.

Net realized gains (losses) on foreign currency transactions represent net foreign exchange gains (losses) from foreign currency exchange contracts, disposition of foreign currencies, currency gains (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

## **Morgan Stanley Emerging Markets Domestic Debt Fund, Inc.**

**October 31, 2012**

### Notes to Financial Statements (cont'd)

liabilities at period end exchange rates are reflected as a component of unrealized 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, which are denominated in foreign currencies. Such securities 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 issuers may be subject to substantial governmental involvement in the economy and greater social, economic and political uncertainty.

**4. Structured Investments:** The Fund invested a portion of its assets in structured investments. A structured investment is a derivative security designed to offer a return linked to a particular underlying security, currency, commodity or market. Structured investments may come in various forms including notes, warrants and options to purchase securities. The Fund will typically use structured investments to gain exposure to a permitted underlying security, currency, commodity or market when direct access to a market is limited or inefficient from a tax or cost standpoint. Investments in structured investments involve risks including issuer risk, counterparty risk and market risk. Holders of structured investments bear risks of the underlying investment and are subject to issuer or counterparty risk because the Fund is relying on the creditworthiness of such issuer or counterparty and has no

rights with respect to the underlying investment. 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 time, may be unable to find qualified buyers for these securities.

**5. Derivatives:** The Fund may, but is not required to, 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 an underlying asset, interest rate, index or financial instrument. A derivative instrument often has risks similar to its underlying asset and may have additional risks, including imperfect correlation between the value of the derivative and the underlying asset, risks of default by the counterparty 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 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 recognized.

Certain derivative transactions may give rise to a form of leverage. Leverage magnifies the potential for gain and risk for loss. 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,



**Morgan Stanley Emerging Markets Domestic Debt Fund, Inc.****October 31, 2012**

## Notes to Financial Statements (cont'd)

pursuant to applicable Securities and Exchange Commission rules and regulations, or may cause the Fund to be more volatile than if the Fund had not been leveraged. Although the 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 used during the period and their associated risks:

**Foreign Currency Exchange Contracts:** In connection with its investments in foreign securities, the Fund also entered into contracts with banks, brokers or dealers to purchase or sell securities or foreign currencies at a future date. A foreign currency exchange contract ("currency contracts") is a negotiated agreement between two parties to exchange specified amounts of two or more currencies at a specified future time at a specified rate. The rate specified by the currency contract can be higher or lower than the spot rate between the currencies that are the subject of the contract. Currency 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. Hedging the Fund's currency risks involves the risk of mismatching the Fund's objectives under a currency 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 currency contracts. The use of currency contracts involves the risk of loss from the insolvency or bankruptcy of the counterparty to the contract or the failure of the

counterparty to make payments or otherwise comply with the terms of the contract. A currency 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 currency contract is closed equal to the difference between the value of the currency contract at the time it was opened and the value at the time it was closed.

FASB ASC 815, "Derivatives and Hedging: Overall" ("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 October 31, 2012.

<b>Primary Risk Exposure</b>	<b>Statement of Assets and Liabilities</b>	<b>Foreign Currency Exchange Contracts (000)</b>
<b>Assets:</b>		
Currency Risk Unrealized Appreciation on Foreign Currency	Exchange Contracts	\$ 570

**Liabilities:**

Currency Risk Unrealized

Depreciation on

Foreign Currency

Exchange Contracts

\$ (656)

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 October 31, 2012 in accordance with ASC 815.

**Morgan Stanley Emerging Markets Domestic Debt Fund, Inc.****October 31, 2012**

Notes to Financial Statements (cont'd)

	<b>Realized Gain (Loss)</b>	
<b>Primary Risk Exposure</b>	<b>Derivative Type</b>	<b>Value (000)</b>
Currency Risk Foreign Currency	Exchange Contracts	\$ 5,376
	<b>Change in Unrealized Appreciation (Depreciation)</b>	
<b>Primary Risk Exposure</b>	<b>Derivative Type</b>	<b>Value (000)</b>
Currency Risk Foreign Currency	Exchange Contracts	\$(3,602)

For the year ended October 31, 2012, the average monthly principal amount of foreign currency exchange contracts was approximately \$169,252,000.

**6. Indemnifications:** 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.

**7. 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. Dividend income and distributions are recorded on the ex-dividend date (except for certain dividends which may be recorded as soon as the Fund is informed of such dividends) net of applicable withholding taxes.

**B. Advisory Fees:** The Adviser, a wholly-owned subsidiary of Morgan Stanley, provides the Fund with advisory services under the terms of an Investment Advisory Agreement, calculated weekly and payable monthly, at an annual rate of 1.00% of the Fund's average weekly managed assets.

**C. Administration Fees:** The Adviser also serves as Administrator to the Fund and provides administrative services pursuant to an Administration Agreement for an annual fee, accrued daily and paid monthly, of 0.08% of the Fund's average weekly managed assets. Under a Sub-Administration Agreement between the Administrator and State Street Bank and Trust Company ("State Street"), State Street provides certain administrative services to the Fund. For such services, the Administrator pays State Street a portion of the fee the Administrator receives from the Fund.

**D. Custodian Fees:** State Street (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 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. Dividend income and 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. Taxes may also be based on transactions in foreign currency and are accrued based on the value of investments denominated in such currency.

**Morgan Stanley Emerging Markets Domestic Debt Fund, Inc.****October 31, 2012**

## Notes to Financial Statements (cont'd)

FASB ASC 740-10, *Income Taxes* Overall, 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" in the Statement of Operations. The Fund files tax returns with the U.S. Internal Revenue Service, New York and various states. Each of the tax years in the four-year period ended October 31, 2012, remains subject to examination by taxing authorities.

The tax character of distributions paid may differ from the character of distributions shown in 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 2012 and 2011 was as follows:

<b>2012 Distributions</b>		<b>2011 Distributions</b>	
<b>Paid From:</b>		<b>Paid From:</b>	
<b>Ordinary Income (000)</b>	<b>Long-Term Capital Gain (000)</b>	<b>Ordinary Income (000)</b>	<b>Long-Term Capital Gain (000)</b>
\$ 83,296		\$ 86,918	

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 GAAP. These book/tax differences are considered either temporary or permanent in nature.

Temporary differences are attributable to differing book and tax treatments for the timing of the recognition of gains (losses) on certain investment transactions, the timing of the deductibility of certain expenses and the recognition of premium amortization.

Permanent differences, primarily due to differing treatments of gains (losses) related to foreign currency transactions and premium amortization adjustments for certain securities sold, resulted in the following reclassifications among the components of net assets at October 31, 2012:

<b>Accumulated Undistributed Net Investment Income (000)</b>	<b>Accumulated Net Realized Loss (000)</b>	<b>Paid-in- Capital (000)</b>
\$ (16,171)	\$ 16,067	\$ 104

At October 31, 2012, distributable earnings for the Fund on a tax basis were as follows:

<b>Undistributed Ordinary Income (000)</b>	<b>Undistributed Long-Term Capital Gain (000)</b>
\$ 11,840	



At October 31, 2012, the aggregate cost for federal income tax purposes is approximately \$1,657,827,000. The aggregate gross unrealized appreciation is approximately \$67,015,000 and the aggregate gross unrealized depreciation is approximately \$91,788,000 resulting in net unrealized depreciation of approximately \$24,773,000.

On December 22, 2010, the Regulated Investment Company Modernization Act of 2010 (the "Modernization Act") was signed into law. The Modernization Act modernizes several tax provisions related to Regulated Investment Companies ("RICs") and their shareholders. One key change made by the Modernization Act is that capital losses will generally retain their character as short-term or long-term and may be carried forward indefinitely to offset future gains. These losses are utilized before other capital loss carryforwards that expire. Generally, the Modernization Act is effective for taxable years beginning after December 22, 2010.

**Morgan Stanley Emerging Markets Domestic Debt Fund, Inc.****October 31, 2012**

## Notes to Financial Statements (cont'd)

At October 31, 2012, the Fund had available for Federal income tax purposes unused capital losses, which will expire on the indicated dates:

<b>Amount (000)</b>	<b>Expiration</b>
\$ 9,250	October 31, 2017

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. During the year ended October 31, 2012, the Fund utilized capital loss carryforwards for U.S. Federal income tax purposes of approximately \$26,342,000.

**F. Security Transactions and Transactions with Affiliates:** For the year ended October 31, 2012, purchases and sales of investment securities for the Fund, other than long-term U.S. Government securities and short-term investments, were approximately \$1,056,394,000 and \$1,018,117,000, respectively. There were no purchases and sales of long-term U.S. Government securities for the year ended October 31, 2012.

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. 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 investments in the Liquidity Funds. For the year ended October 31, 2012, advisory fees paid were reduced by approximately \$22,000 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 October 31, 2012 is as follows:

<b>Value October 31, 2011 (000)</b>	<b>Purchases at Cost (000)</b>	<b>Sales (000)</b>	<b>Dividend Income (000)</b>	<b>Value October 31, 2012 (000)</b>
\$ 3,822	\$ 237,314	\$ 222,501	\$ 25	\$ 18,635

The Fund has an unfunded Deferred Compensation Plan (the "Compensation Plan"), which allows each independent Director to defer payment of all, or a portion, of the fees he or she receives for serving on the Board of Directors. Each eligible Director generally may elect to have the deferred amounts credited with a return equal to the total return on one or more of the Morgan Stanley funds that are offered as investment options under the Compensation Plan. Appreciation/depreciation and distributions received from these investments are recorded with an offsetting increase/decrease in the deferred compensation obligation and do not affect the net asset value of the Fund.

**G. Credit Facility:** The Fund will use the proceeds from the use of leverage to purchase additional securities consistent with the Fund's investment objectives, policies and strategies. The Fund has engaged JPMorgan Securities Inc. to arrange a syndicate of lenders to provide a revolving line of credit facility ("facility") in the amount of \$400,000,000. The term of the facility is 364 days and the loans under the facility will bear interest at the rate of LIBOR for the applicable interest period plus a spread. The loans will be secured by a fully perfected first priority lien on all of the assets of the Fund capable of being pledged. The facility also has a commitment fee of 0.20% of the daily

unused portion of the facility. The facility was set to expire in April 2012. It was extended for 30 days and then renewed for another 364 days until May 2013. The average borrowings and interest rate for the year ended October 31, 2012 were approximately \$396,328,000 and 1.75%, respectively, during a period of 364 days. During the same period, the Fund incurred

**Morgan Stanley Emerging Markets Domestic Debt Fund, Inc.****October 31, 2012**

Notes to Financial Statements (cont'd)

approximately \$7,061,000 in interest expense associated with the outstanding loans.

**H. Other:** On January 10, 2008, the Fund commenced a share repurchase program for purposes of enhancing stockholder value and reducing the discount at which the Fund's shares trade from their net asset value per share ("NAV"). During the year ended October 31, 2012, the Fund did not repurchase any of its shares. Since the inception of the program, the Fund has repurchased 886,200 of its shares at an average discount of 23.87% from NAV. The Directors regularly monitor the Fund's share repurchase program as part of their review and consideration of the Fund's premium/discount history. The Fund expects to continue to repurchase its outstanding shares at such time and in such amounts as it believes will further the accomplishment of the foregoing objectives, subject to review by the Directors.

**I. Results of Annual Meeting of Stockholders (unaudited):** On July 24, 2012, an annual meeting of the Fund's stockholders was held for the purpose of voting on the following matter, the results of which were as follows:

Election of Directors by all stockholders:

	<b>For</b>	<b>Withheld</b>
Michael Bozic	63,346,513	2,768,953
Michael F. Klein	63,483,773	2,631,693
W. Allen Reed	63,081,769	3,033,697

**J. Accounting Pronouncement:** In December 2011, FASB issued Accounting Standards Update ("ASU") 2011-11, Balance Sheet: Disclosures about Offsetting Assets and Liabilities. The pronouncement improves disclosures for recognized financial and derivative instruments that are either offset on the balance sheet in accordance with the offsetting guidance in ASC 210-20-45, Balance Sheet: Offsetting Other Presentation Matters or ASC 815-10-45, Derivatives: Overall Other Presentation Matters or are subject to enforceable master netting agreements or similar agreements.

The Fund will be required to disclose information about rights to offset and related arrangements (such as collateral agreements) in order to enable financial statement users to understand the effect of those rights and arrangements on its financial position as well as disclose the following (1) gross amounts; (2) amounts offset in the statement of financial position; (3) any other amounts that can be offset in the event of bankruptcy, insolvency or default of any of the parties (including cash and noncash financial collateral); and (4) the Fund's net exposure. The requirements are effective for annual reporting periods beginning on or after January 1, 2013, and must be applied retrospectively. At this time, the Fund's management is evaluating the implications of ASU 2011-11 and its impact, if any, on the financial statements.

**Morgan Stanley Emerging Markets Domestic Debt Fund, Inc.**

**October 31, 2012**

Notes to Financial Statements (cont'd)

**For More Information About Portfolio Holdings (unaudited)**

The Fund provides a complete schedule of portfolio holdings in its semi-annual and annual reports within 60 days of the end of the Fund's second and fourth fiscal quarters. The semi-annual reports and the annual reports are filed electronically with the Securities and Exchange Commission (SEC) on Form N-CSRS and Form N-CSR, respectively. Morgan Stanley also delivers the semi-annual and annual reports to Fund stockholders and makes these reports available on its public website, [www.morganstanley.com/im](http://www.morganstanley.com/im). Each Morgan Stanley fund also files a complete schedule of portfolio holdings with the SEC for the Fund's first and third fiscal quarters on Form N-Q. Morgan Stanley does not deliver the reports for the first and third fiscal quarters to stockholders, nor are the reports posted to the Morgan Stanley public website. You may, however, obtain the Form N-Q filings (as well as the Form N-CSR and N-CSRS filings) by accessing the SEC's website, [www.sec.gov](http://www.sec.gov). You may also review and copy them at the SEC's Public Reference Room in Washington, DC. Information on the operation of the SEC's Public Reference Room may be obtained by calling the SEC toll free at 1(800) SEC-0330. You can also request copies of these materials, upon payment of a duplicating fee, by electronic request at the SEC's e-mail address ([publicinfo@sec.gov](mailto:publicinfo@sec.gov)) or by writing the public reference section of the SEC, Washington, DC 20549-0102.

In addition to filing a complete schedule of portfolio holdings with the SEC each fiscal quarter, the Fund makes portfolio holdings information available by periodically providing the information on its public website, [www.morganstanley.com/im](http://www.morganstanley.com/im).

The Fund provides a complete schedule of portfolio holdings on the public website on a calendar-quarter basis approximately 31 calendar days after the close of the calendar quarter. The Fund also provides Top 10 holdings information on the public website approximately 15 business days following the end of each month. You may obtain copies of the Fund's monthly or calendar-quarter website postings, by calling toll free 1(800) 231-2608.

**Proxy Voting Policy and Procedures and Proxy Voting Record (unaudited)**

A copy of (1) the Fund's policies and procedures with respect to the voting of proxies relating to the Fund's portfolio securities; and (2) how the Fund voted proxies relating to portfolio securities during the most recent twelve-month period ended June 30, is available without charge, upon request, by calling toll free 1(800) 548-7786 or by visiting our website at [www.morganstanley.com/im](http://www.morganstanley.com/im). This information is also available on the SEC's web site at [www.sec.gov](http://www.sec.gov).



**Morgan Stanley Emerging Markets Domestic Debt Fund, Inc.**

**October 31, 2012**

Report of Independent Registered Public Accounting Firm

**To the Stockholders and Board of Directors of  
Morgan Stanley Emerging Markets Domestic Debt Fund, Inc.**

We have audited the accompanying statement of assets and liabilities of Morgan Stanley Emerging Markets Domestic Debt Fund, Inc. (the "Fund"), including the portfolio of investments, as of October 31, 2012, and the related statements of operations and cash flows for the year then ended, the statements of changes in net assets for each of the two years in the period then ended, and the financial highlights for each of the five years in the period then ended. These financial statements and financial highlights are the responsibility of the Fund's management. Our responsibility is to express an opinion on these financial statements and financial highlights based on our audits.

We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements and financial highlights are free of material misstatement. We were not engaged to perform an audit of the Fund's internal control over financial reporting. Our audits included consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Fund's internal control over financial reporting. Accordingly, we express no such opinion. An audit also includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements and financial highlights, assessing the accounting principles used and significant estimates made by management, and evaluating the overall financial statement presentation. Our procedures included confirmation of securities owned as of October 31, 2012, by correspondence with the custodian and others. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements and financial highlights referred to above present fairly, in all material respects, the financial position of Morgan Stanley Emerging Markets Domestic Debt Fund, Inc. at October 31, 2012, and the results of its statements of operations and cash flows for the year then ended, the changes in its net assets for each of the two years in the period then ended, and the financial highlights for each of the five years in the period then ended, in conformity with U.S. generally accepted accounting principles.

Boston, Massachusetts  
December 21, 2012

**Morgan Stanley Emerging Markets Domestic Debt Fund, Inc.**

**October 31, 2012**

Portfolio Management (unaudited)

The Fund is managed by members of the Emerging Markets Debt team. The team consists of portfolio managers and analysts. Current members of the team jointly and primarily responsible for the day-to-day management of the Fund's portfolio are Eric J. Baurmeister and Federico L. Kaune, each a Managing Director of the Adviser. Mr. Baurmeister has been associated with the Adviser in an investment management capacity since 1997 and began managing the Fund at its inception. Mr. Kaune has been associated with the Adviser in an investment management capacity since 2002 and began managing the Fund at its inception.



## **Morgan Stanley Emerging Markets Domestic Debt Fund, Inc.**

**October 31, 2012**

### Investment Policy (unaudited)

The Fund may, but is not required to, 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 an underlying asset, interest rate, index or financial instrument. A derivative instrument often has risks similar to its underlying asset and may have additional risks, including imperfect correlation between the value of the derivative and the underlying asset, risks of default by the counterparty 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. Certain derivative transactions may give rise to a form of leverage. Leverage magnifies the potential for gain and risk of loss. 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 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:

*Foreign Currency Exchange 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. A foreign currency exchange contract ("currency contract") is a negotiated agreement between two parties to exchange specified amounts of two or more currencies at a specified future time at a specified rate. The rate specified by the currency contract can be higher or lower than the spot rate between the currencies that are the subject of the contract. Currency 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. Hedging the Fund's currency risks involves the risk of mismatching the Fund's objectives under a currency 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. The use of currency contracts involves the risk of loss from the insolvency or bankruptcy of the counterparty to the contract or the failure of the counterparty to make payments or otherwise comply with the terms of the contract.

*Futures.* A futures contract is a standardized, exchange-traded agreement to buy or sell a specific quantity of an underlying asset, reference rate or index 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. 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



**Morgan Stanley Emerging Markets Domestic Debt Fund, Inc.**

**October 31, 2012**

Investment Policy (unaudited) (cont'd)

the settlement date. 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 contracts 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.* 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 at an agreed-upon price typically in exchange for a premium paid by the Fund. If the Fund sells an option, it sells to another person 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. 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.

*Structured Investments.* The Fund also may invest a portion of its assets in structured investments. A structured investment is a derivative security designed to offer a return linked to a particular underlying security, currency, commodity or market. Structured investments may come in various forms including notes, warrants and options to purchase securities. The Fund will typically use structured investments to gain exposure to a permitted underlying security, currency, commodity or market when direct access to a market is limited or inefficient from a tax or cost standpoint. Investments in structured investments involve risks including issuer risk, counterparty risk and market risk. Holders of structured investments bear risks of the underlying investment and are subject to issuer or counterparty risk because the Fund is relying on the creditworthiness of such issuer or counterparty and has no rights with respect to the underlying investment. 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.

*Swaps.* An over-the-counter ("OTC") swap contract 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, currencies or other instruments. A small percentage of swap contracts are cleared through a central clearinghouse. 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 contract 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 party. Most swap agreements are not entered into or traded on exchanges and often there is no central clearing or guaranty function for swaps. These OTC swaps are often 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.

**Morgan Stanley Emerging Markets Domestic Debt Fund, Inc.**

**October 31, 2012**

Dividend Reinvestment Plan (unaudited)

Pursuant to the Dividend Reinvestment Plan (the Plan), each stockholder will be deemed to have elected, unless Computershare Trust Company, N.A. (the Plan Agent) is otherwise instructed by the stockholder in writing, to have all distributions automatically reinvested in Fund shares.

Dividend and capital gain distributions (Distribution) will be reinvested on the reinvestment date in full and fractional shares. If the market price per share equals or exceeds net asset value per share on the reinvestment date, the Fund will issue shares to participants at net asset value or, if net asset value is less than 95% of the market price on the reinvestment date, shares will be issued at 95% of the market price. If net asset value exceeds the market price on the reinvestment date, participants will receive shares valued at market price. The Fund may purchase shares of its Common Stock in the open market in connection with dividend reinvestment requirements at the discretion of the Board of Directors. Should the Fund declare a Distribution payable only in cash, the Plan Agent will purchase Fund shares for participants in the open market as agent for the participants.

The Plan Agent's fees for the reinvestment of a Distribution will be paid by the Fund. However, each participant's account will be charged a pro rata share of brokerage commissions incurred on any open market purchases effected on such participant's behalf. Although stockholders in the Plan may receive no cash distributions, participation in the Plan will not relieve participants of any income tax which may be payable on such dividends or distributions.

In the case of stockholders, such as banks, brokers or nominees, that hold shares for others who are the beneficial owners, the Plan Agent will administer the Plan on the basis of the number of shares certified from time to time by the stockholder as representing the total amount registered in the stockholder's name and held for the account of beneficial owners who are participating in the Plan.

Stockholders who do not wish to have Distributions automatically reinvested should notify the Plan Agent in writing. There is no penalty for non-participation or withdrawal from the Plan, and stockholders who have previously withdrawn from the Plan may rejoin at any time. Requests for additional information or any correspondence concerning the Plan should be directed to the Plan Agent at:

Morgan Stanley Emerging Markets Domestic Debt Fund, Inc.  
Computershare Trust Company, N.A.  
P.O. Box 43078  
Providence, Rhode Island 02940-3078  
1 (800) 231-2608

## **Morgan Stanley Emerging Markets Domestic Debt Fund, Inc.**

**October 31, 2012**

U.S. Privacy Policy (unaudited)

### **An Important Notice Concerning Our U.S. Privacy Policy**

*This privacy notice describes the U.S. privacy policy of Morgan Stanley Distribution, Inc., and the Morgan Stanley family of mutual funds ("us", "our", "we").*

We are required by federal law to provide you with notice of our U.S. privacy policy ("Policy"). This Policy applies to both our current and former clients unless we state otherwise and is intended for individual clients who purchase products or receive services from us for personal, family or household purposes. This Policy is not applicable to partnerships, corporations, trusts or other non-individual clients or account holders, nor is this Policy applicable to individuals who are either beneficiaries of a trust for which we serve as trustee or participants in an employee benefit plan administered or advised by us. This Policy is, however, applicable to individuals who select us to be a custodian of securities or assets in individual retirement accounts, 401(k) accounts, or accounts subject to the Uniform Gifts to Minors Act.

This notice sets out our business practices to protect your privacy; how we collect and share personal information about you; and how you can limit our sharing or certain uses by others of this information. We may amend this Policy at any time, and will inform you of any changes to our Policy as required by law.

### **We Respect Your Privacy**

We appreciate that you have provided us with your personal financial information and understand your concerns about your information. We strive to safeguard the information our clients entrust to us. Protecting the confidentiality and security of client information is an important part of how we conduct our business.

This notice describes what personal information we collect about you, how we collect it, when we may share it with others, and how certain others may use it. It discusses the steps you may take to limit our sharing of certain information about you with our affiliated companies, including, but not limited to our affiliated banking businesses, brokerage firms and credit service affiliates. It also discloses how you may limit our affiliates' use of shared information for marketing purposes.

Throughout this Policy, we refer to the nonpublic information that personally identifies you as "personal information." We also use the term "affiliated company" in this notice. An affiliated company is a company in our family of companies and includes companies with the Morgan Stanley name. These affiliated companies are financial institutions such as broker-dealers, banks, investment advisers and credit card issuers. We refer to any company that is not an affiliated company as a nonaffiliated third party. For purposes of Section 5 of this notice, and your ability to limit certain uses of personal information by our affiliates, this notice applies to the use of personal information by our affiliated companies.

### **1. What Personal Information Do We Collect From You?**

We may collect the following types of information about you: (i) information provided by you, including information from applications and other forms we receive from you, (ii) information about your transactions with us or our affiliates, (iii) information



## **Morgan Stanley Emerging Markets Domestic Debt Fund, Inc.**

**October 31, 2012**

U.S. Privacy Policy (unaudited) (cont'd)

about your transactions with nonaffiliated third parties, (iv) information from consumer reporting agencies, (v) information obtained from our websites, and (vi) information obtained from other sources. For example:

- We collect information such as your name, address, e-mail address, telephone/fax numbers, assets, income and investment objectives through applications and other forms you submit to us.
- We may obtain information about account balances, your use of account(s) and the types of products and services you prefer to receive from us through your dealings and transactions with us and other sources.
- We may obtain information about your creditworthiness and credit history from consumer reporting agencies.
- We may collect background information from and through third-party vendors to verify representations you have made and to comply with various regulatory requirements.

### **2. When Do We Disclose Personal Information We Collect About You?**

*We may disclose personal information we collect about you in each of the categories listed above to affiliated and nonaffiliated third parties.*

**a. Information We Disclose to Affiliated Companies.** We may disclose personal information that we collect about you to our affiliated companies to manage your account(s) effectively, to service and process your transactions, and to let you know about products and services offered by us and affiliated companies, to manage our business, and as otherwise required or permitted by law. Offers for products and services from affiliated companies are developed under conditions designed to safeguard your personal information.

**b. Information We Disclose to Third Parties.** We may disclose personal information that we collect about you to nonaffiliated third parties to provide marketing services on our behalf or to other financial institutions with whom we have joint marketing agreements. We may also disclose all of the information we collect to other nonaffiliated third parties for our everyday business purposes, such as to process transactions, maintain account(s), respond to court orders and legal investigations, report to credit bureaus, offer our own products and services, protect against fraud, for institutional risk control, to perform services on our behalf, and as otherwise required or permitted by law.

When we share personal information about you with a nonaffiliated third party, they are required to limit their use of personal information about you to the particular purpose for which it was shared and they are not allowed to share personal information about you with others except to fulfill that limited purpose or as may be permitted or required by law.

## **Morgan Stanley Emerging Markets Domestic Debt Fund, Inc.**

**October 31, 2012**

U.S. Privacy Policy (unaudited) (cont'd)

### **3. How Do We Protect the Security and Confidentiality of Personal Information We Collect About You?**

We maintain physical, electronic and procedural security measures that comply with applicable law and regulations to help safeguard the personal information we collect about you. We have internal policies governing the proper handling of client information by employees. Third parties that provide support or marketing services on our behalf may also receive personal information about you, and we require them to adhere to appropriate security standards with respect to such information.

### **4. How Can You Limit Our Sharing Certain Personal Information About You With Our Affiliated Companies for Eligibility Determination?**

By following the opt-out procedures in Section 6 below, you may limit the extent to which we share with our affiliated companies, personal information that was collected to determine your eligibility for products and services such as your credit reports and other information that you have provided to us or that we may obtain from third parties ("eligibility information"). Eligibility information does not include your identification information or personal information pertaining to our transactions or experiences with you. Please note that, even if you direct us not to share eligibility information with our affiliated companies, we may still share your personal information, including eligibility information, with our affiliated companies under circumstances that are permitted under applicable law, such as to process transactions or to service your account.

### **5. How Can You Limit the Use of Certain Personal Information About You by Our Affiliated Companies for Marketing?**

By following the opt-out instructions in Section 6 below, you may limit our affiliated companies from marketing their products or services to you based on personal information we disclose to them. This information may include, for example, your income and account history with us. Please note that, even if you choose to limit our affiliated companies from using personal information about you that we may share with them for marketing their products and services to you, our affiliated companies may use your personal information that they obtain from us to market to you in circumstances permitted by law, such as if the affiliated party has its own relationship with you.

### **6. How Can You Send Us an Opt-Out Instruction?**

If you wish to limit our sharing of eligibility information about you with our affiliated companies, or our affiliated companies' use of personal information for marketing purposes, as described in this notice, you may do so by:

- Calling us at (800) 548-7786  
Monday - Friday between 8a.m. and 5p.m. (EST)

- Writing to us at the following address:

Morgan Stanley Services Company Inc.  
c/o Privacy Coordinator  
201 Plaza Two, 3rd Floor



Jersey City, New Jersey 07311

## **Morgan Stanley Emerging Markets Domestic Debt Fund, Inc.**

**October 31, 2012**

### **U.S. Privacy Policy (unaudited) (cont'd)**

If you choose to write to us, your request should include: your name, address, telephone number and account number(s) to which the opt-out applies and whether you are opting out with respect to sharing of eligibility information (Section 4 above), or information used for marketing (Section 5 above), or both. Written opt-out requests should not be sent with any other correspondence. In order to process your request, we require that the request be provided by you directly and not through a third party. Once you have informed us about your privacy preferences, your opt-out preference will remain in effect with respect to this Policy (as it may be amended) until you notify us otherwise. If you are a joint account owner, we will accept instructions from any one of you and apply those instructions to the entire account.

Please understand that if you limit our sharing or our affiliated companies' use of personal information, you and any joint account holder(s) may not receive information about our affiliated companies' products and services, including products or services that could help you manage your financial resources and achieve your investment objectives.

If you have more than one account or relationship with us, please specify the accounts to which you would like us to apply your privacy choices. If you have accounts or relationships with our affiliates, you may receive multiple privacy policies from them, and will need to separately notify those companies of your privacy choices for those accounts or relationships.

### **7. What if an affiliated company becomes a nonaffiliated third party?**

If, at any time in the future, an affiliated company becomes a nonaffiliated third party, further disclosures of personal information made to the former affiliated company will be limited to those described in Section 2(b) above relating to nonaffiliated third parties. If you elected under Section 6 to limit disclosures we make to affiliated companies, or use of personal information by affiliated companies, your election will not apply to use by any former affiliated company of your personal information in their possession once it becomes a nonaffiliated third party.

### **SPECIAL NOTICE TO RESIDENTS OF VERMONT**

**The following section supplements our Policy with respect to our individual clients who have a Vermont address and supersedes anything to the contrary in the above Policy with respect to those clients only.**

The State of Vermont requires financial institutions to obtain your consent prior to sharing personal information that they collect about you with nonaffiliated third parties, or eligibility information with affiliated companies, other than in certain limited circumstances. Except as permitted by law, we will not share personal information we collect about you with nonaffiliated third parties or eligibility information with affiliated companies, unless you provide us with your written consent to share such information.

### **SPECIAL NOTICE TO RESIDENTS OF CALIFORNIA**

**The following section supplements our Policy with respect to our individual clients who have a California address and supersedes anything to the contrary in the above Policy with respect to those clients only.**

In response to a California law, if your account has a California home address, your personal information will not be disclosed to nonaffiliated third parties except as permitted by applicable California law, and we will limit sharing such

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personal information with our affiliates to comply with California privacy laws that apply to us.



**Morgan Stanley Emerging Markets Domestic Debt Fund, Inc.**

**October 31, 2012**

Director and Officer Information (unaudited)

Independent Director:

Name, Age and Address	Position(s) of Held	Length of Time Served*	Principal Occupation(s) During Past 5 Years	Number of Portfolios in Fund Complex Overseen by	Other Directorships Held by Independent Director***
Frank L. Bowman (68) c/o Kramer Levin Naftalis & Frankel LLP Counsel to the Independent Directors 1177 Avenue of the Americas New York, NY 10036	Director	Since August 2006	President, Strategic Decisions, LLC (consulting) (since February 2009); Director or Trustee of various Morgan Stanley Funds (since August 2006); Chairperson of the Insurance Sub-Committee of the Compliance and Insurance Committee (since February 2007); served as President and Chief Executive Officer of the Nuclear Energy Institute (policy organization) (February 2005-November 2008); retired as Admiral, U.S. Navy after serving over 38 years on active duty including 8 years as Director of the Naval Nuclear Propulsion Program in the Department of the Navy and the U.S. Department of Energy (1996-2004); served as Chief of Naval Personnel (July 1994-September 1996); and on the Joint Staff as Director of Political Military Affairs (June 1992-July 1994); Knighted as Honorary Knight Commander of the Most Excellent Order of the British Empire; Awarded the Officer de l'Orde National du Mérite by the French Government; elected to the National Academy of Engineering	102	Director of BP p.l.c.; Director of Naval and Nuclear Technologies LLP; Director of the Armed Services YMCA of the USA and the Naval Submarine League; Director of the American Shipbuilding Suppliers Association; Member of the National Security Advisory Council of the Center for U.S. Global Engagement and a member of the CNA Military Advisory Board; Member of the American Lung Association's President's Council.

Michael Bozic (71) c/o Kramer Levin Naftalis & Frankel LLP Counsel to the Independent Directors 1177 Avenue of the Americas New York, NY 10036	Director since April 1994	(2009). Private investor; Chairperson of the Compliance and Insurance Committee (since October 2006); Director or Trustee of various Morgan Stanley Funds (since April 1994); formerly, Chairperson of the Insurance Committee (July 2006-September 2006); Vice Chairman of Kmart Corporation (December 1998-October 2000), Chairman and Chief Executive Officer of Levitz Furniture Corporation (November 1995-November 1998) and President and Chief Executive Officer of Hills Department Stores (May 1991-July 1995); variously Chairman, Chief Executive Officer, President and Chief Operating Officer (1987-1991) of the Sears Merchandise Group of Sears, Roebuck & Co.	104 Director of various business organizations.
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**Morgan Stanley Emerging Markets Domestic Debt Fund, Inc.**

**October 31, 2012**

Director and Officer Information (unaudited) (cont'd)

Independent Director (cont'd):

Name, Age and Address	Position(s) of Held	Length of Time Served*	Principal Occupation(s) During Past 5 Years	Number of Portfolios in Fund Complex Overseen by	Other Directorships Held by Independent Director***
Kathleen A. Dennis (59) c/o Kramer Levin Naftalis & Frankel LLP Counsel to the Independent Directors 1177 Avenue of the Americas New York, NY 10036	Director	Since August 2006	President, Cedarwood Associates (mutual fund and investment management consulting) (since July 2006); Chairperson of the Money Market and Alternatives Sub-Committee of the Investment Committee (since October 2006) and Director or Trustee of various Morgan Stanley Funds (since August 2006); formerly, Senior Managing Director of Victory Capital Management (1993-2006).	102	Director of various non-profit organizations.
Dr. Manuel H. Johnson (63) c/o Johnson Smick Group,	Director	Since July 1991	Senior Partner, Johnson Smick International, Inc. (consulting firm); Chairperson of the Investment Committee (since October 2006) and Director or Trustee of various Morgan Stanley Funds (since July 1991); Co-Chairman and a founder of the Group of Seven Council (G7C) (international economic	104	Director of NVR, Inc. (home construction).

Inc.  
888  
16th  
Street,  
N.W.  
Suite  
740  
Washington,  
D.C.  
20006

commission); formerly, Chairperson  
of the Audit Committee (July  
1991-September 2006), Vice  
Chairman of the Board of  
Governors of the Federal Reserve  
System and Assistant Secretary of  
the U.S. Treasury.

Joseph Directo since  
J. August  
Kearns 1994  
(70)  
c/o  
Kearns  
&  
Associates  
LLC  
PMB754  
22631  
Pacific  
Coast  
Highway  
Malibu,  
CA  
90265

President, Kearns & Associates  
LLC (investment consulting);  
Chairperson of the Audit Committee  
(since October 2006) and Director  
or Trustee of various Morgan  
Stanley Funds (since August 1994);  
formerly, Deputy Chairperson of the  
Audit Committee (July  
2003-September 2006) and  
Chairperson of the Audit Committee  
of various Morgan Stanley Funds  
(since August 1994); CFO of the J.  
Paul Getty Trust.

105 Director of Electro Rent Corporation  
(equipment leasing) and The Ford  
Family Foundation.



**Morgan Stanley Emerging Markets Domestic Debt Fund, Inc.****October 31, 2012**

Director and Officer Information (unaudited) (cont'd)

Independent Director (cont'd):

Name, Age and Address	Position (Length of Held of with Time Registered Since	Principal Occupation(s) During Past 5 Years	Number of Portfolios in Fund Complex Overseen by Independent Director**	Other Directorships Held by Independent Director***
Michael F. Klein (54) c/o Kramer Levin Naftalis & Frankel LLP Counsel to the Independent Directors 1177 Avenue of the Americas New York, NY 10036	Director Since August 2006	Managing Director, Aetos Capital, LLC (since March 2000) and Co-President, Aetos Alternatives Management, LLC (since January 2004); Chairperson of the Fixed Income Sub-Committee of the Investment Committee (since October 2006) and Director or Trustee of various Morgan Stanley Funds (since August 2006); formerly, Managing Director, Morgan Stanley & Co. Inc. and Morgan Stanley Dean Witter Investment Management, President, various Morgan Stanley Funds (June 1998-March 2000) and Principal, Morgan Stanley & Co. Inc. and Morgan Stanley Dean Witter Investment Management (August 1997-December 1999).	102	Director of certain investment funds managed or sponsored by Aetos Capital, LLC. Director of Sanitized AG and Sanitized Marketing AG (specialty chemicals).
Michael E. Nugent (76) c/o	Chairperson of the Boards Since and July	General Partner, Triumph Capital, L.P. (private investment partnership); Chairperson of the Boards of various Morgan Stanley	104	None.

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<p>Triumph Capital, L.P. 445 Park Avenue New York, NY 10022</p>	<p>Director and Director since July 1991</p>	<p>2006 Funds (since July 2006); Chairperson of the Closed-End Fund Committee (since June 2012) and Director or Trustee of various Morgan Stanley Funds (since July 1991); formerly, Chairperson of the Insurance Committee (until July 2006).</p>	
<p>W. Allen Reed (65) c/o Kramer Levin Naftalis &amp; Frankel LLP Counsel to the Independent Directors 1177 Avenue of the Americas New York, NY 10036</p>	<p>Director Since August 2006</p>	<p>Chairperson of the Equity Sub-Committee of the Investment Committee (since October 2006) and Director or Trustee of various Morgan Stanley Funds (since August 2006); formerly, President and CEO of General Motors Asset Management; Chairman and Chief Executive Officer of the GM Trust Bank and Corporate Vice President of General Motors Corporation (August 1994-December 2005).</p>	<p>102 Director of Temple-Inland Industries (packaging and forest products); Director of Legg Mason, Inc. and Director of the Auburn University Foundation.</p>
<p>Ferguson Reid (80) c/o Joe Pietryka, Inc. 85 Charles Colman Blvd. Pawling, NY 12564</p>	<p>Director Since June 1992</p>	<p>Chairman, Joe Pietryka, Inc.; Chairperson of the Governance Committee and Director or Trustee of various Morgan Stanley Funds (since June 1992).</p>	<p>105 Trustee and Director of certain investment companies in the JPMorgan Funds complex managed by JP Morgan Investment Management Inc.</p>



**Morgan Stanley Emerging Markets Domestic Debt Fund, Inc.**

**October 31, 2012**

Director and Officer Information (unaudited) (cont'd)

Interested Director:

Name, Age and Address	Position(s) of Held	Length of Time Served*	Principal Occupation(s) During Past 5 Years	Number of Portfolios in Fund Complex Overseen by Director**	Other Directorships Held by Interested Director***
James F. Higgins (64) c/o Morgan Stanley Services Company Inc. Harborside Financial Center 201 Plaza Two Jersey City, NJ 07311	Director	Since June 2000	Director or Trustee of various Morgan Stanley Funds (since June 2000); Senior Advisor of Morgan Stanley (since August 2000).	103	Director of AXA Financial, Inc. and The Equitable Life Assurance Society of the United States (financial services).

\* Each Director serves an indefinite term, until his or her successor is elected.

\*\* The Fund Complex includes (as of December 31, 2011) all open-end and closed-end funds (including all of their portfolios) advised by Morgan Stanley Investment Management Inc. (the "Adviser") and any funds that have an adviser that is an affiliated person of the Adviser (including, but not limited to, Morgan Stanley AIP GP LP).

\*\*\* This includes any directorships at public companies and registered investment companies held by the Director at any time during the past five years.



**Morgan Stanley Emerging Markets Domestic Debt Fund, Inc.****October 31, 2012**

Director and Officer Information (unaudited) (cont'd)

Executive Officers:

Name, Age and Address of Executive Officer	Position(s) Held with Registrant	Length of Time Served*	Principal Occupation(s) During Past 5 Years
Arthur Lev (51) 522 Fifth Avenue New York, NY 10036	President and Principal Executive Officer Equity and Fixed Income Funds	Since June 2011	President and Principal Executive Officer (since June 2011) of the Equity and Fixed Income Funds in the Fund Complex; Head of the Long Only Business of Morgan Stanley Investment Management (since February 2011); Managing Director of the Adviser and various entities affiliated with the Adviser (since December 2006). Formerly, Chief Strategy Officer of Morgan Stanley Investment Management's Traditional Asset Management business (November 2010-February 2011); General Counsel of Morgan Stanley Investment Management (December 2006-October 2010); Partner and General Counsel of FrontPoint Partners LLC (July 2002-December 2006); Managing Director and General Counsel of Morgan Stanley Investment Management (May 2000-June 2002).
Mary Ann Picciotto (39) c/o Morgan Stanley Services Company Inc. Harborside Financial Center 201 Plaza Two Jersey City, NJ 07311	Chief Compliance Officer	Since May 2010	Managing Director of the Adviser and various entities affiliated with the Adviser; Chief Compliance Officer of various Morgan Stanley Funds (since May 2010); Chief Compliance Officer of the Adviser (since April 2007).
Stefanie V. Chang Yu (46) 522 Fifth Avenue	Vice President	Since December 1997	Managing Director of the Adviser and various entities affiliated with the Adviser; Vice President of various Morgan Stanley Funds (since December 1997).

New York,  
NY 10036

Francis J. Smith (47) c/o Morgan Stanley Services Company Inc. Harborside Financial Center 201 Plaza Two Jersey City, NJ 07311	Treasurer and Principal Financial Officer	Treasurer since July 2003 and Principal Financial Officer since September 2002	Executive Director of the Adviser and various entities affiliated with the Adviser; Treasurer and Principal Financial Officer of various Morgan Stanley Funds (since July 2003).
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Harborside  
Financial  
Center  
201 Plaza  
Two  
Jersey  
City, NJ  
07311

Mary E. Mullin (45) 522 Fifth Avenue New York, NY 10036	Secretary	Since June 1999	Executive Director of the Adviser and various entities affiliated with the Adviser; Secretary of various Morgan Stanley Funds (since June 1999).
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\* Each officer serves an indefinite term, until his or her successor is elected.





Item 2. Code of Ethics.

(a) The Trust/Fund has adopted a code of ethics (the Code of Ethics ) that applies to its principal executive officer, principal financial officer, principal accounting officer or controller, or persons performing similar functions, regardless of whether these individuals are employed by the Trust/Fund or a third party.

(b) No information need be disclosed pursuant to this paragraph.

(c) Not applicable.

(d) Not applicable.

(e) Not applicable.

(f)

(1) The Trust/Fund's Code of Ethics is attached hereto as Exhibit 12 A.

(2) Not applicable.

(3) Not applicable.

Item 3. Audit Committee Financial Expert.

The Fund's Board of Trustees has determined that Joseph J. Kearns, an independent Trustee, is an audit committee financial expert serving on its audit committee. Under applicable securities laws, a person who is determined to be an audit committee financial expert will not be deemed an expert for any purpose, including without limitation for the purposes of Section 11 of the Securities Act of 1933, as a result of being designated or identified as an audit committee financial expert. The designation or identification of a person as an audit committee financial expert does not impose on such person any duties, obligations, or liabilities that are greater than the duties, obligations, and liabilities imposed on such person as

a member of the audit committee and Board of Trustees in the absence of such designation or identification.

Item 4. Principal Accountant Fees and Services.

(a)(b)(c)(d) and (g). Based on fees billed for the periods shown:

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2012

	Registrant	Covered Entities(1)
<b>Audit Fees</b>	\$ 86,800	N/A
<b>Non-Audit Fees</b>		
<b>Audit-Related Fees</b>	\$ (2)	\$ 201,000(2)
<b>Tax Fees</b>	\$ 3,380(3)	\$ 854,999(4)
<b>All Other Fees</b>	\$	\$
<b>Total Non-Audit Fees</b>	\$ 3,380	\$ 1,055,099
<b>Total</b>	\$ 90,180	\$ 1,055,099

2011

	Registrant	Covered Entities(1)
<b>Audit Fees</b>	\$ 86,800	N/A
<b>Non-Audit Fees</b>		
<b>Audit-Related Fees</b>	\$ (2)	\$ (2)
<b>Tax Fees</b>	\$ 3,380(3)	\$ 89,626(4)
<b>All Other Fees</b>	\$	\$ 390,354(5)
<b>Total Non-Audit Fees</b>	\$ 3,380	\$ 479,980
<b>Total</b>	\$ 90,180	\$ 479,980

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N/A- Not applicable, as not required by Item 4.

(1) Covered Entities include the Adviser (excluding sub-advisors) and any entity controlling, controlled by or under common control with the Adviser that provides ongoing services to the Registrant.

(2) Audit-Related Fees represent assurance and related services provided that are reasonably related to the performance of the audit of the financial statements of the Covered Entities and funds advised by the Adviser or its affiliates, specifically data verification and agreed-upon procedures related to asset securitizations and agreed-upon procedures engagements.

(3) Tax Fees represent tax compliance, tax planning and tax advice services provided in connection with the preparation and review of the Registrant's tax returns.

(4) Tax Fees represent tax compliance, tax planning and tax advice services provided in connection with the review of Covered Entities' tax returns.

(5) All other fees represent project management for future business applications and improving business and operational processes.

(e)(1) The audit committee's pre-approval policies and procedures are as follows:

**APPENDIX A**

**AUDIT COMMITTEE**  
**AUDIT AND NON-AUDIT SERVICES**  
**PRE-APPROVAL POLICY AND PROCEDURES**  
**OF THE**  
**MORGAN STANLEY RETAIL AND INSTITUTIONAL FUNDS**  
  
**AS ADOPTED AND AMENDED JULY 23, 2004,(1)**

**1. Statement of Principles**

The Audit Committee of the Board is required to review and, in its sole discretion, pre-approve all Covered Services to be provided by the Independent Auditors to the Fund and Covered Entities in order to assure that services performed by the Independent Auditors do not impair the auditor's independence from the Fund.

The SEC has issued rules specifying the types of services that an independent auditor may not provide to its audit client, as well as the audit committee's administration of the engagement of the independent auditor. The SEC's rules establish two different approaches to pre-approving services, which the SEC considers to be equally valid. Proposed services either: may be pre-approved without consideration of specific case-by-case services by the Audit Committee (general pre-approval); or require the specific pre-approval of the Audit Committee or its delegate (specific pre-approval). The Audit Committee believes that the combination of these two approaches in this Policy will result in an effective and efficient procedure to pre-approve services performed by the Independent Auditors. As set forth in this Policy, unless a type of service has received general pre-approval, it will require specific pre-approval by the Audit Committee (or by any member of the Audit Committee to which pre-approval authority has been delegated) if it is to be provided by the Independent Auditors. Any proposed services exceeding pre-approved cost levels or budgeted amounts will also require specific pre-approval by the Audit Committee.

The appendices to this Policy describe the Audit, Audit-related, Tax and All Other services that have the general pre-approval of the Audit Committee. The term of any general pre-approval is 12 months from the date of pre-approval, unless the Audit Committee considers and provides a different period and states otherwise. The Audit Committee will annually review and pre-approve the services that may be provided by the Independent Auditors without obtaining specific pre-approval from the Audit Committee. The Audit Committee will add to or subtract from the list of general pre-approved services from time to time, based on subsequent determinations.

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(1) This Audit Committee Audit and Non-Audit Services Pre-Approval Policy and Procedures (the Policy ), adopted as of the date above, supersedes and replaces all prior versions that may have been adopted from time to time.

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The purpose of this Policy is to set forth the policy and procedures by which the Audit Committee intends to fulfill its responsibilities. It does not delegate the Audit Committee's responsibilities to pre-approve services performed by the Independent Auditors to management.

The Fund's Independent Auditors have reviewed this Policy and believes that implementation of the Policy will not adversely affect the Independent Auditors' independence.

## **2. Delegation**

As provided in the Act and the SEC's rules, the Audit Committee may delegate either type of pre-approval authority to one or more of its members. The member to whom such authority is delegated must report, for informational purposes only, any pre-approval decisions to the Audit Committee at its next scheduled meeting.

## **3. Audit Services**

The annual Audit services engagement terms and fees are subject to the specific pre-approval of the Audit Committee. Audit services include the annual financial statement audit and other procedures required to be performed by the Independent Auditors to be able to form an opinion on the Fund's financial statements. These other procedures include information systems and procedural reviews and testing performed in order to understand and place reliance on the systems of internal control, and consultations relating to the audit. The Audit Committee will approve, if necessary, any changes in terms, conditions and fees resulting from changes in audit scope, Fund structure or other items.

In addition to the annual Audit services engagement approved by the Audit Committee, the Audit Committee may grant general pre-approval to other Audit services, which are those services that only the Independent Auditors reasonably can provide. Other Audit services may include statutory audits and services associated with SEC registration statements (on Forms N-1A, N-2, N-3, N-4, etc.), periodic reports and other documents filed with the SEC or other documents issued in connection with securities offerings.

The Audit Committee has pre-approved the Audit services in Appendix B.1. All other Audit services not listed in Appendix B.1 must be specifically pre-approved by the Audit Committee (or by any member of the Audit Committee to which pre-approval has been delegated).

## **4. Audit-related Services**

Audit-related services are assurance and related services that are reasonably related to the performance of the audit or review of the Fund's financial statements and, to the extent they are Covered Services, the Covered Entities or that are traditionally performed by the Independent Auditors. Because the Audit Committee believes that the provision of Audit-related services does not impair the independence of the auditor and is consistent with the SEC's rules on auditor independence, the Audit Committee may grant general pre-approval to Audit-related services. Audit-related services include, among others, accounting consultations related to accounting, financial reporting or disclosure matters



not classified as Audit services ; assistance with understanding and implementing new accounting and financial reporting guidance from rulemaking authorities; agreed-upon or expanded audit procedures related to accounting and/or billing records required to respond to or comply with financial, accounting or regulatory reporting matters; and assistance with internal control reporting requirements under Forms N-SAR and/or N-CSR.

The Audit Committee has pre-approved the Audit-related services in Appendix B.2. All other Audit-related services not listed in Appendix B.2 must be specifically pre-approved by the Audit Committee (or by any member of the Audit Committee to which pre-approval has been delegated).

## **5. Tax Services**

The Audit Committee believes that the Independent Auditors can provide Tax services to the Fund and, to the extent they are Covered Services, the Covered Entities, such as tax compliance, tax planning and tax advice without impairing the auditor's independence, and the SEC has stated that the Independent Auditors may provide such services.

Pursuant to the preceding paragraph, the Audit Committee has pre-approved the Tax Services in Appendix B.3. All Tax services in Appendix B.3 must be specifically pre-approved by the Audit Committee (or by any member of the Audit Committee to which pre-approval has been delegated).

## **6. All Other Services**

The Audit Committee believes, based on the SEC's rules prohibiting the Independent Auditors from providing specific non-audit services, that other types of non-audit services are permitted. Accordingly, the Audit Committee believes it may grant general pre-approval to those permissible non-audit services classified as All Other services that it believes are routine and recurring services, would not impair the independence of the auditor and are consistent with the SEC's rules on auditor independence.

The Audit Committee has pre-approved the All Other services in Appendix B.4. Permissible All Other services not listed in Appendix B.4 must be specifically pre-approved by the Audit Committee (or by any member of the Audit Committee to which pre-approval has been delegated).

## **7. Pre-Approval Fee Levels or Budgeted Amounts**

Pre-approval fee levels or budgeted amounts for all services to be provided by the Independent Auditors will be established annually by the Audit Committee. Any proposed services exceeding these levels or amounts will require specific pre-approval by the Audit Committee. The Audit Committee is mindful of the overall relationship of fees for audit and non-audit services in determining whether to pre-approve any such services.



**8. Procedures**

All requests or applications for services to be provided by the Independent Auditors that do not require specific approval by the Audit Committee will be submitted to the Fund's Chief Financial Officer and must include a detailed description of the services to be

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rendered. The Fund's Chief Financial Officer will determine whether such services are included within the list of services that have received the general pre-approval of the Audit Committee. The Audit Committee will be informed on a timely basis of any such services rendered by the Independent Auditors. Requests or applications to provide services that require specific approval by the Audit Committee will be submitted to the Audit Committee by both the Independent Auditors and the Fund's Chief Financial Officer, and must include a joint statement as to whether, in their view, the request or application is consistent with the SEC's rules on auditor independence.

The Audit Committee has designated the Fund's Chief Financial Officer to monitor the performance of all services provided by the Independent Auditors and to determine whether such services are in compliance with this Policy. The Fund's Chief Financial Officer will report to the Audit Committee on a periodic basis on the results of its monitoring. Both the Fund's Chief Financial Officer and management will immediately report to the chairman of the Audit Committee any breach of this Policy that comes to the attention of the Fund's Chief Financial Officer or any member of management.

## **9. Additional Requirements**

The Audit Committee has determined to take additional measures on an annual basis to meet its responsibility to oversee the work of the Independent Auditors and to assure the auditor's independence from the Fund, such as reviewing a formal written statement from the Independent Auditors delineating all relationships between the Independent Auditors and the Fund, consistent with Independence Standards Board No. 1, and discussing with the Independent Auditors its methods and procedures for ensuring independence.

## **10. Covered Entities**

Covered Entities include the Fund's investment adviser(s) and any entity controlling, controlled by or under common control with the Fund's investment adviser(s) that provides ongoing services to the Fund(s). Beginning with non-audit service contracts entered into on or after May 6, 2003, the Fund's audit committee must pre-approve non-audit services provided not only to the Fund but also to the Covered Entities if the engagements relate directly to the operations and financial reporting of the Fund. This list of Covered Entities would include:

### Morgan Stanley Retail Funds

Morgan Stanley Investment Advisors Inc.

Morgan Stanley & Co. Incorporated

Morgan Stanley DW Inc.

Morgan Stanley Investment Management Inc.

Morgan Stanley Investment Management Limited

Morgan Stanley Investment Management Private Limited

Morgan Stanley Asset & Investment Trust Management Co., Limited

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Morgan Stanley Investment Management Company

Morgan Stanley Services Company, Inc.

Morgan Stanley Distributors Inc.

Morgan Stanley Trust FSB

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Morgan Stanley Institutional Funds

Morgan Stanley Investment Management Inc.

Morgan Stanley Investment Advisors Inc.

Morgan Stanley Investment Management Limited

Morgan Stanley Investment Management Private Limited

Morgan Stanley Asset & Investment Trust Management Co., Limited

Morgan Stanley Investment Management Company

Morgan Stanley & Co. Incorporated

Morgan Stanley Distribution, Inc.

Morgan Stanley AIP GP LP

Morgan Stanley Alternative Investment Partners LP

(e)(2) Beginning with non-audit service contracts entered into on or after May 6, 2003, the audit committee also is required to pre-approve services to Covered Entities to the extent that the services are determined to have a direct impact on the operations or financial reporting of the Registrant. 100% of such services were pre-approved by the audit committee pursuant to the Audit Committee's pre-approval policies and procedures (attached hereto).

(f) Not applicable.

(g) See table above.

(h) The audit committee of the Board of Trustees has considered whether the provision of services other than audit services performed by the auditors to the Registrant and Covered Entities is compatible with maintaining the auditors' independence in performing audit services.

Item 5. Audit Committee of Listed Registrants.

(a) The Fund has a separately-designated standing audit committee established in accordance with Section 3(a)(58)(A) of the Exchange Act whose members are:

Joseph Kearns, Michael Nugent and Allen Reed.

(b) Not applicable.

Item 6.

(a) See Item 1.

(b) Not applicable.

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Item 7. Disclosure of Proxy Voting Policies and Procedures for Closed-End Management Investment Companies.

The Fund/Trust invests in exclusively non-voting securities and therefore this item is not applicable.

Item 8. Portfolio Managers of Closed-End Management Investment Companies

Applicable only to reports filed by closed-end funds.

**Morgan Stanley Emerging Markets Domestic Debt Fund, Inc.**

**FUND MANAGEMENT**

**PORTFOLIO MANAGEMENT.** As of the date of this report, the Fund is managed by members of the Emerging Markets Debt team. The team consists of portfolio managers and analysts. Current members of the team jointly and primarily responsible for the day-to-day management of the Fund's portfolio are Eric J. Baurmeister and Federico L. Kaune, each a Managing Director of the Adviser.

Mr. Baurmeister has been associated with the Adviser in an investment management capacity since October 1997 and began managing the Fund at its inception. Mr. Kaune has been associated with the Adviser in an investment management capacity since August 2002 and began managing the Fund at its inception. Mr. Baurmeister and Mr. Kaune are co-portfolio managers. Certain other members of the team collaborate to manage the assets of the Fund, but are not primarily responsible for the day-to-day management of the Fund.

The composition of the team may change from time to time.

**OTHER ACCOUNTS MANAGED BY THE PORTFOLIO MANAGERS**

As of October 31, 2012:

Mr. Baurmeister managed seven registered investment companies with a total of approximately \$2.5 billion in assets; 10 pooled investment vehicles other than registered investment companies with a total of approximately \$2.4 billion in assets; and 11 other accounts with a total of approximately \$5.4 billion in assets. Of these other accounts, one account with a total of approximately \$301.3 million in assets, had performance-based fees.

Mr. Kaune managed six registered investment companies with a total of approximately \$2.5 billion in assets; 10 pooled investment vehicles other than registered investment companies with a total of approximately \$2.4 billion in assets; and 11 other accounts with a total of approximately \$5.4 billion in assets. Of these other accounts, one account with a total of approximately \$301.3 million in assets, had performance-based fees.

Because the portfolio managers manages assets for other investment companies, pooled investment vehicles and/or other accounts (including institutional clients, pension plans and certain high net worth individuals), there may be an incentive to favor one client over another resulting in conflicts of interest. For instance, the Adviser may receive fees from certain accounts that are higher than the fee it receives from the Fund, or it may receive a performance-based fee on certain accounts. In those instances, the portfolio

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manager may have an incentive to favor the higher and/or performance-based fee accounts over the Fund. In addition, a conflict of interest could exist to the extent the Adviser has proprietary investments in certain accounts, where portfolio managers have personal investments in certain accounts or when certain accounts are investment options in the Adviser's employee benefits and/or deferred compensation plans. The portfolio managers may have an incentive to favor these accounts over others. If the Adviser manages accounts that engage in short sales of securities of the type in which the Fund invests, the Adviser could be seen as harming the performance of the Fund for the benefit of the accounts engaging in short sales if the short sales cause the market value of the securities to fall. The Adviser has adopted trade allocation and other policies and procedures that it believes are reasonably designed to address these and other conflicts of interest.

#### PORTFOLIO MANAGER COMPENSATION STRUCTURE

Portfolio managers receive a combination of base compensation and discretionary compensation, comprising a cash bonus and several deferred compensation programs described below. The methodology used to determine portfolio manager compensation is applied across all funds/accounts managed by the portfolio managers.

**BASE SALARY COMPENSATION.** Generally, portfolio managers receive base salary compensation based on the level of their position with the Adviser.

**DISCRETIONARY COMPENSATION.** In addition to base compensation, portfolio managers may receive discretionary compensation.

Discretionary compensation can include:

- Cash Bonus.
- Morgan Stanley's Long Term Incentive Compensation awards - a mandatory program that defers a portion of discretionary year-end compensation into restricted stock units or other awards based on Morgan Stanley common stock or other plans that are subject to vesting and other conditions. All long-term incentive compensation awards are subject to clawback provisions where awards can be cancelled if an employee takes any action, or omits to take any action which causes a restatement of Morgan Stanley's consolidated financial results, or constitutes a violation of Morgan Stanley's risk policies and standards.
- Investment Management Alignment Plan (IMAP) awards - a mandatory program that defers a portion of discretionary year-end compensation and notionally invests it in designated funds advised by the Adviser or its affiliates. The award is subject to vesting and other conditions. Portfolio managers must notionally invest a minimum of 25% to a maximum of 100% of their IMAP deferral account into a combination of the designated funds they manage that are included in the IMAP fund menu, which may or may not include the Fund. In addition to the clawbacks listed above for long-term incentive compensation awards, the provision on IMAP awards is further strengthened such that it may also be triggered if an employee's actions cause substantial financial loss on the trading strategy, investment, commitment or other holding provided that previous gains on those positions were relevant to the employee's prior year compensation decisions.



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- Voluntary Deferred Compensation Plans - voluntary programs that permit certain employees to elect to defer a portion of their discretionary year-end compensation and notionally invest the deferred amount across a range of designated investment funds, which may include funds advised by the Adviser or its affiliates.

Several factors determine discretionary compensation, which can vary by portfolio management team and circumstances. These factors include:

- Revenues generated by the investment companies, pooled investment vehicles and other accounts managed by the portfolio manager.
-

- Contribution to the business objectives of the Adviser.
- The dollar amount of assets managed by the portfolio manager.
- Market compensation survey research by independent third-parties.
- Other qualitative factors, such as contributions to client objectives.
- Performance of Morgan Stanley and Morgan Stanley Investment Management, and the overall performance of the investment team(s) of which the portfolio manager is a member.

SECURITIES OWNERSHIP OF PORTFOLIO MANAGERS

As of October 31, 2012, the portfolio managers did not own any shares of the Fund.

Item 9. Closed-End Fund Repurchases

REGISTRANT PURCHASE OF EQUITY SECURITIES

Period	(a) Total Number of Shares (or Units) Purchased	(b) Average Price Paid per Share (or Unit)	(c) Total Number of Shares (or Units) Purchased as Part of Publicly Announced Plans or Programs	(d) Maximum Number (or Approximate Dollar Value) of Shares (or Units) that May Yet Be Purchased Under the Plans or Programs
mo-da-year				
mo-da-year			N/A	N/A
mo-da-year				
mo-da-year			N/A	N/A
mo-da-year				
mo-da-year			N/A	N/A
mo-da-year			N/A	N/A



Item 10. Submission of Matters to a Vote of Security Holders

Not applicable.

Item 11. Controls and Procedures

(a) The Trust s/Fund s principal executive officer and principal financial officer have concluded that the Trust s/Fund s disclosure controls and procedures are sufficient to ensure that information required to be disclosed by the Trust/Fund in this Form N-CSR was recorded, processed, summarized and reported within the time periods specified in the Securities and Exchange Commission s rules and forms, based upon such officers evaluation of these controls and procedures as of a date within 90 days of the filing date of the report.

(b) There were no changes in the registrant s internal control over financial reporting that occurred during the second fiscal quarter of the period covered by this report that has materially affected, or is reasonably likely to materially affect, the registrant s internal control over financial reporting.

Item 12. Exhibits

(a) The Code of Ethics for Principal Executive and Senior Financial Officers is attached hereto.

(b) A separate certification for each principal executive officer and principal financial officer of the registrant are attached hereto as part of EX-99.CERT.

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**SIGNATURES**

Pursuant to the requirements of the Securities Exchange Act of 1934 and the Investment Company Act of 1940, the registrant has duly caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

Morgan Stanley Emerging Markets Domestic Debt

/s/ Arthur Lev  
Arthur Lev  
Principal Executive Officer  
December 13, 2012

Pursuant to the requirements of the Securities Exchange Act of 1934 and the Investment Company Act of 1940, this report has been signed by the following persons on behalf of the registrant and in the capacities and on the dates indicated.

/s/ Arthur Lev  
Arthur Lev  
Principal Executive Officer  
December 13, 2012

/s/ Francis Smith  
Francis Smith  
Principal Financial Officer  
December 13, 2012

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