

MORGAN STANLEY EMERGING MARKETS DEBT FUND INC
Form N-CSR
March 10, 2011

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

FORM N-CSR

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

Investment Company Act file number 811-07694

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

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

10036
(Zip code)

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

Registrant's telephone number, including area code: 212-296-6990

Date of fiscal year end: December 31, 2010

Date of reporting period: December 31, 2010

Item 1 - Report to Shareholders

Morgan Stanley Emerging Markets Debt Fund, Inc.

Directors

Michael E. Nugent

Frank L. Bowman

Michael Bozic

Kathleen A. Dennis

James F. Higgins

Dr. Manuel H. Johnson

Joseph J. Kearns

Michael F. Klein

W. Allen Reed

Fergus Reid

Officers

Michael E. Nugent

Chairman of the Board and Director

Sara Furber

*President and Principal
Executive Officer*

Stefanie V. Chang Yu

Vice President

Francis J. Smith

Treasurer and Principal Financial Officer

Mary Ann Picciotto

Chief Compliance Officer

Mary E. Mullin

Secretary

Investment Adviser and Administrator

Morgan Stanley Investment Management Inc.

522 Fifth Avenue

New York, New York 10036

Custodian

State Street Bank and Trust Co.

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. All investments involve risks, including the possible loss of principal.

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IU11-00345P-Y12/10

INVESTMENT MANAGEMENT

Morgan Stanley

Emerging Markets Debt

Fund, Inc. (MSD)

Morgan Stanley

Investment Management Inc.

Investment Adviser

**Annual
Report**

December 31, 2010

Morgan Stanley Emerging Markets Debt Fund, Inc.

Overview (unaudited)

Letter to Stockholders

Performance

For the year ended December 31, 2010, the Morgan Stanley Emerging Markets Debt Fund, Inc. (the "Fund") had total returns of 11.00%, based on net asset value, and 13.58% based on market value per share (including reinvestment of distributions), compared to its benchmark, the J.P. Morgan Emerging Markets Bond Global Index (the "Index"), which returned 12.04%. On December 31, 2010, the closing price of the Fund's shares on the New York Stock Exchange was \$10.48, representing a 7.9% discount to the Fund's net asset value per share. Past performance is no guarantee of future results.

Factors Affecting Performance

- The first quarter of 2010 was overall a good period for fixed income assets, which were supported by a positive macro backdrop of benign economic data and unchanged monetary policy in the G-3. In addition, important policy decisions influenced global markets including the passage of U.S. health care reform, and sovereign risk related issues especially around Greece and peripheral Europe. Against this backdrop, emerging markets (EM) debt strongly outperformed developed markets debt in the first quarter.
- Financial markets remained choppy throughout the second quarter of 2010 as investors focused on the unfolding crisis in peripheral Europe. Worries over a potential "double dip" recession and banking sector struggles in the developed world, and tighter monetary policies in certain EM countries overshadowed the generally strong fundamentals in the U.S. and most of the EM world. During the quarter, EM central banks stepped up the movement toward the normalization of monetary policy. Such actions highlighted the inner strength of most emerging countries.
- During the third quarter, EM debt markets continued to be driven primarily by economic and policy developments in the developed world, rather than by EM-centered events. EM central banks slowed the pace of rate hikes as growth softened from very robust levels and inflation remained stable. EM debt continued to benefit from strong portfolio inflows.
- Performance of risky assets through the fourth quarter of 2010 as a whole was driven by two opposing factors. The first, which was consistent with greater appetite for risk, involved moves by policy makers in the U.S. that aimed to boost economic growth in 2011. The most obvious initiatives were the second round of quantitative easing (QE2) and the extension of the Bush-era tax cuts. However, sentiment soured and appetite for risk fell in November as a result of the fiscal crisis in Ireland. Emerging markets debt, like most risky assets, generally underperformed during the last three months of the year. Nevertheless, in relation to other episodes in which global investors have become risk averse, the negative returns were modest, coinciding with EM data flow confirming that fundamentals remain intact and favorable.
- EM hard currency debt, as measured by the J.P. Morgan Emerging Markets Bond Global Index, returned 12.04% for 2010. As of December 31, 2010, external debt yields stood at 6.13%, with a spread of 289 basis points above U.S. Treasuries.
- For the year, our strategy benefited from yield curve positioning in Colombia, Peru, Kazakhstan and Indonesia as well as to local rates to South Africa, Turkey, Brazil and Mexico. An overweight exposure to Argentina and Ukraine

also aided returns.

Morgan Stanley Emerging Markets Debt Fund, Inc.

Overview (unaudited)

Letter to Stockholders (cont'd)

Conversely, yield curve positioning in external debt in Lebanon, Malaysia, Poland, South Africa, Turkey and Uruguay hurt returns. A slight underweight in Brazil and foreign exchange exposure to Hungary also detracted from relative returns.

Management Strategies

- We expect growth in the developed world to recover somewhat in 2011, reflecting a new wave of expansionary fiscal and monetary policies particularly in the U.S. However, the unresolved fiscal sustainability issues in the periphery of Europe and individual states in the U.S. are likely to generate periodic bouts of risk aversion into 2011. Such expansionary policies in the developed world are likely to provide further support to commodity prices and capital inflows to EM countries, but will also exacerbate inflationary and currency appreciation pressures.
- Our constructive view on EM assets in 2011 reflects expectations for strong domestic demand-driven growth, supportive terms of trade and large capital inflows. EM countries are likely to respond to expansionary policies in the developed world by hardening capital controls to avoid a further appreciation of their currencies, while hiking rates at a pace adequate to contain inflationary pressures in their economies. Overall, we believe that EM central banks will be able to slow but not to reverse the appreciation trend in their currencies.
- The impact of the strong macroeconomic fundamentals in the emerging markets on sovereign risk premium appears to be fully priced in most countries, with pockets of undervaluation on which we will focus. In contrast, we believe that higher carry and continued portfolio flows will continue to support EM currencies. Several currencies in Asia and certain commodity currencies remain undervalued and could benefit further from a benign external environment and easy monetary policy in the developed world.

Sincerely,

Sara Furber
President and Principal Executive Officer January 2011

Morgan Stanley Emerging Markets Debt Fund, Inc.

December 31, 2010

Portfolio of Investments

(Showing Percentage of Total Value of Investments)

	Face Amount (000)	Value (000)
FIXED INCOME SECURITIES (86.8%)		
Argentina (4.7%)		
Sovereign (4.7%)		
Argentina Bonos, 7.00%, 10/3/15	\$ 13,689	\$ 12,978
Republic of Argentina, 2.50%, 12/31/38 (a)	2,188	990
8.28%, 12/31/33 (b)	346	323
		14,291
Belarus (0.2%)		
Sovereign (0.2%)		
Republic of Belarus, 8.75%, 8/3/15	710	729
Brazil (8.8%)		
Corporate Bond (0.6%)		
Gerdau Trade, Inc., 5.75%, 1/30/21 (b)(c)	1,700	1,713
Sovereign (8.2%)		
Banco Nacional de Desenvolvimento, Economico e Social, 5.50%, 7/12/20 (c)	1,960	2,024
6.37%, 6/16/18 (c)	1,380	1,509
Federative Republic of Brazil, 5.88%, 1/15/19	9,125	10,174
7.13%, 1/20/37 (b)	590	707
8.00%, 1/15/18	1,527	1,795
8.88%, 10/14/19 - 4/15/24	6,564	8,750
		24,959
		26,672
Colombia (3.1%)		
Sovereign (3.1%)		
Republic of Colombia, 7.38%, 3/18/19 (b)	3,900	4,700
11.75%, 2/25/20	3,015	4,560
		9,260
Croatia (0.5%)		
Sovereign (0.5%)		

Republic of Croatia, 6.63%, 7/14/20 (c)	1,340	1,386
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	Face Amount (000)	Value (000)
Dominican Republic (0.4%)		
Sovereign (0.4%)		
Dominican Republic, 7.50%, 5/6/21 (c)	\$ 590	\$ 638
9.04%, 1/23/18	470	536
		1,174
Ecuador (0.7%)		
Sovereign (0.7%)		
Republic of Ecuador, 9.38%, 12/15/15	2,235	2,090
Georgia (0.3%)		
Sovereign (0.3%)		
Republic of Georgia, 7.50%, 4/15/13	940	970
Ghana (1.1%)		
Sovereign (1.1%)		
Republic of Ghana, 8.50%, 10/4/17 (b)(c)	2,016	2,273
8.50%, 10/4/17	800	908
		3,181
Hungary (0.8%)		
Sovereign (0.8%)		
Hungary Government Bond, 7.50%, 11/12/20	HUF 507,590	2,369
India (0.3%)		
Corporate Bond (0.3%)		
Reliance Holdings USA, Inc., 6.25%, 10/19/40 (c)	\$ 810	813
Indonesia (4.8%)		
Corporate Bonds (0.4%)		
Pindo Deli Finance Mauritius Ltd., Tranche A, 3.29%, 4/28/15 (c)(d)(e)	421	103
Tranche B, 3.29%, 4/28/18 (c)(d)(e)	1,852	204
Tranche C, Zero Coupon, 4/28/27 (c)(d)(e)	7,471	168

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

Morgan Stanley Emerging Markets Debt Fund, Inc.

December 31, 2010

Portfolio of Investments (cont'd)

(Showing Percentage of Total Value of Investments)

	Face Amount (000)	Value (000)
Indonesia (cont'd)		
Corporate Bonds (cont'd)		
Tjiwi Kimia Finance Mauritius Ltd., Tranche A, 3.29%, 4/28/15 (d)(e)	\$ 1,404	\$ 351
Tranche B, 3.29%, 4/28/18 (c)(d)(e)	1,621	316
Tranche C, Zero Coupon, 4/28/27 (c)(d)(e)	3,620	127
		1,269
Sovereign (4.4%)		
Majapahit Holding BV, 7.75%, 1/20/20	2,500	2,894
Republic of Indonesia, 6.88%, 1/17/18	1,000	1,165
7.75%, 1/17/38 (c)	1,353	1,658
11.63%, 3/4/19 (c)	2,169	3,226
11.63%, 3/4/19	2,850	4,239
		13,182
		14,451
Ivory Coast (0.4%)		
Sovereign (0.4%)		
Ivory Coast, 2.50%, 12/31/32 (a)	2,713	1,221
Kazakhstan (3.2%)		
Sovereign (3.2%)		
Development Bank of Kazakhstan JSC, 5.50%, 12/20/15 (b)(c)	1,250	1,266
Intergas Finance BV, 6.38%, 5/14/17	700	738
KazMunayGas National Co., 6.38%, 4/9/21 (b)(c)	2,430	2,421
9.13%, 7/2/18 (c)	3,080	3,619
9.13%, 7/2/18	1,400	1,645
		9,689
Lithuania (1.1%)		

Sovereign (1.1%)

Republic of Lithuania, 6.75%, 1/15/15 (c)	1,200	1,302
7.38%, 2/11/20	1,790	1,989
		3,291

	Face Amount (000)	Value (000)
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Malaysia (1.0%)**Sovereign (1.0%)**

Malaysia Government Bond, 3.21%, 5/31/13	MYR 8,960	\$ 2,913
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Mexico (10.5%)**Sovereign (10.5%)**

Mexican Bonos, 8.00%, 6/11/20	MXN 61,932	5,396
Pemex Project Funding Master Trust, 6.63%, 6/15/35	\$ 2,566	2,624
6.63%, 6/15/38 (b)	1,750	1,786
8.63%, 12/1/23	1,990	2,438
Petroleos Mexicanos, 5.50%, 1/21/21 (b)	5,430	5,525
8.00%, 5/3/19 (b)	1,750	2,117
United Mexican States, 5.63%, 1/15/17 (b)	419	466
5.95%, 3/19/19	3,782	4,236
6.05%, 1/11/40 (b)	1,760	1,808
6.75%, 9/27/34	4,674	5,282
		31,678

Pakistan (0.4%)**Sovereign (0.4%)**

Republic of Pakistan, 6.88%, 6/1/17	1,550	1,356
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Panama (2.0%)**Sovereign (2.0%)**

Republic of Panama, 5.20%, 1/30/20	1,810	1,928
7.13%, 1/29/26 (b)	1,140	1,377
8.88%, 9/30/27	483	664
9.38%, 4/1/29 (b)	1,569	2,208
		6,177

Peru (5.1%)**Sovereign (5.1%)**

Republic of Peru, 7.13%, 3/30/19 (b)	1,890	2,268
7.35%, 7/21/25 (b)	2,410	2,944
8.20%, 8/12/26	PEN 13,260	5,607
8.75%, 11/21/33	\$ 3,340	4,601

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

Morgan Stanley Emerging Markets Debt Fund, Inc.

December 31, 2010

Portfolio of Investments (cont'd)

(Showing Percentage of Total Value of Investments)

	Face Amount (000)	Value (000)
Philippines (4.1%)		
Sovereign (4.1%)		
Republic of Philippines, 4.00%, 1/15/21 (b)	\$ 5,506	\$ 5,345
8.38%, 6/17/19	1,491	