U.S. fund managers are rediscovering their passion for Europe—and not just as a vacation destination.

Since the start of the year, American investors have ramped up their bets on European stocks, spurred on by a brightening economic outlook and low interest rates.

The continent’s stock markets became a favored destination last year as the region emerged from a bruising recession. This year, with U.S. stock indexes treading water after a rip-roaring 2013, interest in European stocks has grown further, fund managers say.

Investors have sent $24.3 billion into European equity funds this year through Feb. 19, according to fund tracker EPFR Global. U.S. stock funds have seen $5 billion in outflows.

In the exchange-traded-fund world, three of the top four stock-based funds in terms of investor inflows in 2014 are the Vanguard FTSE Europe, the iShares MSCI EMU and the Vanguard FTSE Developed Markets ETFs—all of which have heavy exposure to Europe. The three have seen a combined $4.23 billion in new money this year, while $19.1 billion has flowed out of the largest U.S. stock ETF, the SPDR S&P 500 fund.
Blue-chip companies from France to the Netherlands are getting a close look from some managers, while other bargain-minded investors are focusing on so-called peripheral nations such as Ireland, Italy, Spain and Portugal, whose markets were hard hit following the European debt crisis of 2011.

"Some of the best, cheaper assets are in the periphery of Europe," said Nigel Hart, manager of the BlackRock International Opportunities Fund, which has $3.5 billion under management.

The Stoxx Europe 600 index is up 2.4% this year, compared with a 0.7% decline in the S&P 500 index of U.S. companies and a 2.9% drop in the 30-stock Dow Jones Industrial Average.

While the so-called core of Europe has recovered most of its recession-era losses, the periphery still has a way to go. Share indexes in Spain and Italy remain below their peaks heading into the global financial crisis of 2008, while broader European gauges and those covering the U.S. have recovered those peaks.

Many European nations are struggling with high unemployment and slack demand for goods and services, but the euro zone's economy has resumed expanding. Inflation remains low and growth tepid, paving the way for easy central-bank policy that many investors believe will likely buoy share prices.

That backdrop contrasts with the U.S., where the economy appears on more solid footing but the Federal Reserve has been paring back the monthly bond purchases that many investors say contributed to the record-setting 2013 rally.

Monetary policy in the U.S. "will likely be something of a headwind for equities," said Jamie Doyle, manager of the International Value Fund at Los Angeles-based Causeway Capital Management, which has $28 billion in assets under management and has a large portfolio of European shares. "But that's not going to be a factor in Europe."

Many portfolio managers are seeking out the biggest names of the European corporate world, saying valuations make them a bargain compared with top U.S. companies.

"You can find several world-class companies in Europe that have depressed prices because of the region," said Charles Shriver, portfolio manager of the $63 million T. Rowe Price Group TROW -0.12% Global Allocation Fund. "But they are top-tier global corporations."

That fund counts oil company Royal Dutch Shell RDSB.LN +0.79% and German pharmaceuticals company Bayer AG BAYN.XE +0.20% among its top holdings.

In the technology sector, favorites include Atos SA, ATO.FR +0.54% a French technology-services company, and Sopra Group, SOP.FR +1.11% a tech consultancy.
At Causeway, Mr. Doyle likes the Anglo-Dutch consumer giant Unilever ULVR.LN +0.04% NV for its strong global exposure and a dividend yield, reflecting the annual payout as a share of the recent stock price, of 3.8%.

That dividend payment is part of what makes Unilever UN +0.23% a better buy than its American peer Procter & Gamble Co. PG +0.06%, which pays a 3.1% dividend, Mr. Doyle said.

"Unilever trades at a discount with a higher dividend yield," Mr. Doyle said.

The discount comes in the price-to-earnings ratio of the two companies. Procter & Gamble shares are trading at 20.85 times the company's earnings over the past 12 months, compared with 16.73 for Unilever.

But with many European stock markets up 20% or more in the past year, the bargains that have attracted bottom-fishers are harder to find, many investors say.

Shares in the Stoxx Europe 600 index are trading at 21.5 times the next 12 months' expected earnings, above its average of 18.2 since 2003, according to Barclays, BARC.LN +1.08%.

"There is a bit of a risk in core Europe that people think there is more value than there really is," said Michael Gavin, head of asset allocation for the Americas at Barclays.

At the same time, the region's recovery remains fragile, raising risks for companies that benefit from consumer spending, such as Unilever. An initial reading on fourth-quarter euro-zone gross domestic product showed modest improvement, but the result remains well below the pace needed to make a dent in near-record-high unemployment.

Inflation unexpectedly fell in January, prompting calls for the European Central Bank to provide additional stimulus to prevent deflation, which could knock the region's fragile recovery off course.

"It isn't all wine and roses," Mr. Doyle said. "Europe has been through an enormous dislocation and continues to struggle with a number of challenges."

Some say that means tilting portfolios toward countries most badly affected by the debt crisis.

The BlackRock International Opportunities Fund has looked to the hardest-hit sectors within those countries. The Irish building company Kingspan Group KSP,DB -0.75% PLC and Dutch international employment services company Randstad Holding RAND.AE +3.18% NV, which has a strong presence in Spain and Greece, were two of the fund's recent buys. They have soared 60% and 46% over the past year, respectively.

The peripheral European nations are "where the opportunities are leading us," Mr. Hart said.

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