Make the squares:

Choose a method:

-averaging the colours of the pixels in the square.

-using shaders

-using some kind of other algorithm

Do I try to make the picture bigger?

Needs to be scalable

How to know which pixels are in the square

About the background reading:

What kind of topics?

- about how to make a good UI  
-images (bitmaps)

-compression? Pixelation

-wpf vs windows forms?

-something about existing cross stitch software?

-editing images in c#?