

How does post-quantum cryptography affect Central Bank Digital Currency?

Lars Hupe¹^[0000-0002-8442-856X] and Makan Rafiee²

¹ Giesecke+Devrient GmbH, Prinzregentenstr. 161, 81677 München, Germany

² secunet Security Networks AG, Kurfürstenstr. 58, 45138 Essen, Germany
`lars.hupe@gi-de.com`, `makan.rafiie@secunet.com`

Abstract. Central Bank Digital Currency (CBDC) is an emerging trend in digital payments, with the vast majority of central banks around the world researching, piloting, or even operating a digital version of cash. While design choices differ broadly, such as accounts vs. tokens, the wallets are generally protected through cryptographic algorithms that safeguard against double spending and ensure non-repudiation. But with the advent of quantum computing, these algorithms are threatened by new attack vectors. To better understand those threats, we conducted a study of typical assets in a CBDC system, describe which ones are most amenable to post-quantum cryptography, and propose an upgrade strategy.

1 Introduction

Over 130 countries are researching, developing, or piloting a Central Bank Digital Currency (CBDC), according to the latest data in Atlantic Council’s CBDC tracker.³ An additional 11 have already launched a CBDC. Although consensus around the precise definition of “launch” has yet to surface, a production system is generally understood to encompass the following criteria:

- continuous and uninterrupted availability for an indefinite amount of time, i.e. no unannounced shutdown,
- real legal tender that can always be exchanged at face value with cash and deposit money,
- no system resets, i.e. holdings will remain valid,
- upgrade and maintenance work requires little to no intervention from users, except for long-term hardware upgrades, similar to the 2-5 year cycle of bank cards and smartphones.

Any CBDC operating within this framework will face a multitude of challenges, including operational, security, and monetary. In this paper, we are focusing on a core security aspect: cryptography. A basic consequence of the aforementioned criteria is that any replacement or upgrade of cryptographic algorithms

³ <https://www.atlanticcouncil.org/cbdctracker/>, accessed 2023-07-26

needs to be carried out in a rolling fashion, where new and old algorithm can coexist for a period of several months to several years, depending on whether the algorithm is used only in software or also in hardware.

Yet, an even more fundamental problem lies within the choice of the cryptographic algorithm.

The current gold standard in asymmetric cryptography, elliptic curves, are well-understood and widely deployed. Even though multiple sets of parameters for elliptic curves exist, they all share broadly similar characteristics regarding key generation, key lengths, and performance. For example, the ECDSA signature standard with an underlying NIST secp256r1 curve is available in the vast majority of programming languages, as well as in dedicated hardware devices such as HSMs or smart card chips. This enables excellent performance, which in turn means that secp256r1 enjoys popularity.

However, all elliptic curves, including secp256r1, are known not to withstand the emerging threat of quantum computing. Their security relies on the discrete logarithm, which cannot be computed efficiently by classical computers. In other words, with today’s methods, it is computationally infeasible to obtain the private key given only the public key. But an algorithm discovered already in the 90s by Peter W. Shor can perform this operation efficiently given sufficiently large quantum computers [14, 16].

Consequently, classical asymmetric cryptographic algorithms are at risk, not only those deployed in CBDCs. While the precise timelines for the hitherto theoretical turning into practical risk are not yet clear, it is strongly advisable that post-quantum cryptography be incorporated into a CBDC’s design. The library of employed cryptographic primitives in digital currencies is huge- extending not only to wallets, but also to technical components of intermediaries, communication channels, and management of CBDC supply.

The goal of this paper is to, therefore, provide insight into the future of cryptography as it applies to CBDC. The rest of the paper is structured as follows: We first give an overview of classical cryptographic algorithms and what they are used for in the CBDC context (Section 2). Then, we introduce the threats that quantum computing poses, as well as post-quantum algorithms that address those threats (Section 3). Equipped with this, we can then examine the cryptography in use for CBDC implementations and match them to appropriate algorithms (Section 4). Finally, we propose an opinionated framework for rolling updates, i.e., to put the earlier insights into practice (Section 5). Over the course of the paper, we will sometimes refer to cryptocurrencies as examples, as they share many cryptographic aspects with CBDC, but are often better researched, owing to their longer time of operation.

Terminology In general, we define “wallets” as containers of digital assets, and more specifically, CBDC. Wallets can be in hardware or software form and manage private key material. Typically, “hardware wallet” refers to a physical device that is in the hands of a user. Naturally, they also require software to operate, but the hardware aspect refers to the security measures (e.g. secure elements in smart cards or other embedded devices). In contrast, “software wallets” can mean

keys managed by some remote server where users access their funds through an app that authenticates towards the wallet’s operator. Note that this distinction becomes blurred in case of self-custodial wallets, where users may use any combination of soft- and/or hardware, including open source or self-written, to manage their own keys. Following the majority opinion across central banks, we exclude this from consideration here.

As for the CBDC model, we follow the standard “token” vs. “account” distinction (see also Section 3.1), but do not assume either for the purpose of the paper, except when otherwise noted. When it becomes necessary in context, the term “token” is assumed to refer to key material that is short-lived.

“Central bank register” or “register” for short, refers to the centralized storage of transaction and/or token records at a central bank, which may or may not be implemented as a DLT. In public cryptocurrencies, this register is typically a proof-of-work or proof-of-stake blockchain. The register is said to “validate” transactions and/or tokens.

2 Classical cryptographic algorithms

When shifting payments from physical cash to digital assets, a multitude of cryptographic primitives must be employed to control for security requirements. We will first sketch the security requirements and then explain which cryptographic primitives are used to satisfy them.

2.1 Security requirements for cash and digital assets

When two people engage in a cash transaction, e.g. a customer rendering banknotes to a merchant, a number of security requirements are already controlled for.

First, both the payer’s and the payee’s identities are established merely through personal trust: Both people trust the other person to be the rightful sender (or receiver, respectively) of the payment.

Second, authenticity of the banknotes can be established by haptic and visual properties of the physical objects. In many circumstances, for example, when the paid amount exceeds a certain threshold, a receiving party will employ additional authenticity checks of the banknotes: an ultraviolet lamp, a counting machine, or other devices.

Third, the rightful ownership of the banknotes is proved by merely demonstrating physical possession.

Fourth, and relatedly to the previous point, the payment is completed and settled by change of ownership of the banknotes: the cash physically changes hands.

Fifth, the payer is prevented from double-spending, i.e. using the same banknotes for two concurring payments: as opposed to data, physical objects cannot be cloned.

Finally, in a series of multiple of cash payments, it is impossible for any third party to track the payment patterns.

Applying those security requirements to digital assets, they can be summarized in more technical terms as follows:

1. Authenticity of sender and receiver
2. Authenticity of the asset
3. Proof-of-ownership of the asset
4. Non-repudiation of transactions
5. Prevention of double-spending
6. Privacy

For cash, those requirements can be easily derived from its defining characteristics: its physical nature and it being a bearer instrument.

In contrast, in a digital asset ecosystem, they must be controlled with cryptographic primitives. Note that in cryptocurrencies, the first point is often not guaranteed, whereas in CBDC, some form of identity will typically be established, at least locally between participants.

2.2 Classification of cryptographic primitives for digital assets

To ensure the authenticity of sender and receiver, we employ wallet certificates. Those wallet certificates include some identifier, and are derived by a PKI operated by the central bank. The underlying cryptographic primitive are digital signatures, either based on elliptic curves or RSA. Wallet signatures can also be used to ensure non-repudiation of transactions. (See also Section 5.2 for a more detailed treatment of wallet identifiers in our framework.)

Furthermore, the wallet certificates can also be used to establish an end-to-end encrypted channel between the wallets by using a key exchange algorithm, such as ECDH. The communication channel is then encrypted with a symmetric cipher, e.g. AES-128 GCM.

The authenticity of the tokens must also be checked using digital signatures. This comprises the proof-of-ownership from the sender (which can be checked locally by the receiver), as well as a double-spending check (which relies on global knowledge). Therefore, a verifying instance must be involved. In the case of CBDC, this instance can be centrally operated by the central bank, whereas cryptocurrencies would typically use a DLT. Since a central bank has complete knowledge of the tokens in circulation, we refer to its verifying instance as the “central bank register”.

For CBDC, there is an additional requirement in that the register must communicate the authenticity of a token to the receiver thereof. (In blockchains, this is achieved by the receiver monitoring the newly-added blocks.) Consequently, the register can digitally sign its response using a well-known certificate (see also Section 4.2).

In summary, both symmetric and asymmetric cryptography must be used to control for the security requirements in a CBDC ecosystem.

3 Post-quantum cryptography

In this section, we will explain the new threat model that quantum computing creates for digital currencies, or more generally, any type of digital asset. One of the ways to alleviate this problem is to switch to cryptographic algorithms, some of them novel, that do not suffer from those threats. Therefore, we give an overview of the top contenders in NIST’s standardization competition for such post-quantum algorithms. Alternatively or complementary to that, best practices can be applied to mitigate quantum threats in the short term, which we will discuss here too.

3.1 Threats to digital assets

Let us consider an example: assets in digital currencies are typically represented as public-private keypairs. In the cryptocurrency sphere, the main contenders Bitcoin and Ethereum both use the secp256k1 elliptic curve as a basis. Knowledge of the private key corresponding to some digital assets enables the owner to spend that asset. CBDCs would follow the same or a very similar model. Shor’s algorithm can be used advantageously not just for breaking RSA keys, but also for breaking elliptic curve keys.

Incoming payments require the sender to know the recipient’s public key, which is often referred to as an “address”. Conversely, outgoing payments requires producing a digital signature which uses the private key, but can be validated just with the knowledge of the public key, which is typically recorded in a blockchain (or in the case of CBDC, the register). This allows anyone to send assets to a particular address, but only the rightful owner to spend from that address. Security of one’s assets relies on keeping the private key confidential.

Using classical computers, keeping the private key confidential, but allowing the public key to be known or recorded by third parties, does not threaten security.

However, under a quantum regime, an attacker can use a public key to run Shor’s algorithm, obtaining the corresponding private key. Therefore, the attacker is equipped with the ability to produce valid digital signatures. In consequence, stealing the assets.

When sending assets to a particular address, both Bitcoin and Ethereum do not use the public key directly as an address, but rather a hash of the public key. Fortunately, sufficiently long hashes cannot be easily inverted by quantum computers.⁴ While the assets are at rest, i.e. have been received on an address but not yet spent, a quantum attacker does not have an advantage over a classical

⁴ Symmetric ciphers and cryptographic hash functions do not rely on one-way functions but rather on the speed of searching a large key space. Grover’s algorithm is a quantum algorithm that significantly speeds up the search for keys in a key space. By doubling the key sizes of symmetric encryption algorithms to 256 bits and hash algorithms to 512 bits, even Grover’s algorithm does not pose a threat to symmetric cryptography.

attacker. But as soon as assets are transferred out, the legitimate owner must disclose the public key so that the blockchain network (or in the case of CBDC, the register) can validate the signature. In other words, as soon as the assets are in transit, they are at risk.

3.2 Classical mitigation measures

Not all cryptocurrencies have the same exposure to this threat. Bitcoin, or more broadly speaking, “token-based” (also referred to as “UTxO”) digital assets, discourage reuse of the same public-private keypair, and some variants forbid it outright. The advantage lies within the fact that an outgoing transaction from an address will always consume the entirety of the assets associated with that address. For example, if address A has a balance of 10 €, and its owner wants to send 2 € to address B , the wallet will also move the remaining 8 € to a freshly-generated address C . An attacker breaking the public key of A will not be able to steal any assets, since they are now located at C , its public key not known to the attacker.

However, if a quantum attacker can outperform the payment network, and can break A ’s private key faster than the network or blockchain can validate and finalize the aforementioned payment, they could generate a new transaction, moving parts or all of the funds to another address that is controlled by the attacker.

Ethereum, or more broadly speaking, “account-based” digital assets particularly suffer from this problem, since addresses are routinely reused. In other words, the first time an outgoing transaction is signed from an Ethereum address, all assets at rest in that address are available for subsequent theft from an attacker. According to a 2021 survey by Deloitte, approximately 65% of all Ether in the public Ethereum network are stored in addresses with revealed public keys [2].

To summarize, in the case of public cryptocurrencies, using public key hashes and frequent address rotation are both feasible, albeit not perfect, mitigation strategies [1]. CBDCs with a tighter control through the issuing entity and less public exposure can go further: for example, digital signatures and public keys that are transferred from a wallet to backend systems or to another wallet can be additionally protected by end-to-end transit encryption, such as TLS. Unfortunately, these mitigations are also not perfect and subject to quantum threats. Therefore, for some aspects of a CBDC, it becomes necessary to select truly quantum-safe algorithms.

3.3 NIST competition

The National Institute of Standard and Technology (NIST) has a history of holding competitions to evaluate, select and standardize cryptographic algorithms. The most prominent of those competitions were the Advanced Encryption Standard (AES) standardization process between 1997 and 2000 and the NIST hash function competition between 2007 and 2012 [10, 12] .

Type	PKE/KEM	Signature
Lattice-based	CRYSTALS-Kyber	CRYSTALS-Dilithium FALCON
Hash-based	n/a	SPHINCS+

Table 1. Overview over the winners of the NIST competition

The competition entails multiple rounds with each round eliminating a number of submitted algorithms. Research groups are encouraged to submit algorithms, which are then tested and evaluated by the NIST and the broader scientific community. NIST specifies evaluation criteria for the competition and selects the winning algorithm at the end of the process.

During the leading post-quantum cryptography conference PQCrypto in 2016, the NIST announced a new competition for selecting quantum secure asymmetric cryptographic algorithms [7].

While all previous competitions were designated to select exactly one winning algorithm, such as a symmetric encryption algorithm (AES) or a flexible hash function (SHA-3), this new competition, however, selects multiple new asymmetric algorithms as winners. The algorithms are divided in two subcategories: Public Key Encryption/Key Encapsulation Method and Signature Scheme.

The reason for selecting multiple algorithms as winners is a result of the inevitable drawbacks that these new algorithms will bring: Some are very slow in signature creation, while others have very large key material. Since there is no one-fits-all solution, algorithms must be selected for their specific use cases. Selecting multiple winning algorithms yields greater flexibility in cryptographic agility and enables implementors to tailor the choice of algorithms to their specific needs.

Five mathematical one-way functions turned out to be promising for designing quantum secure algorithms: hash-based, lattice-based, code-based, multivariate polynomial-based and supersingular elliptic curve isogeny-based.

In July 2022, the NIST announced the winners of the competition as well as further algorithms to be considered [11, 13]. Lattice-based algorithms and hash-based signatures were the only one-way functions in the winning algorithms.

The most prominent multivariate and isogeny-based algorithms were both broken last year in a matter of days and fell out of relevance for further consideration [4, 5].

Winners of the NIST competition CRYSTALS-Kyber was the only algorithm selected for PKE/KEM, which does not yield flexibility in the choice of algorithms. Therefore, in the following, we will only consider the advantages and drawbacks of the signature algorithms: CRYSTALS-Dilithium, FALCON and SPHINCS+.

Comparison of signature algorithms In 2020, Sikeridis *et al.* ran a performance study on quantum-secure signature algorithms to analyze and compare key sizes and operational run-time [17].

Size comparison It can be observed that the classical algorithms RSA and ECDSA have remarkably low key and signature sizes, which cannot be reached by the quantum secure alternatives. Only SPHINCS+ has much lower key sizes, which is counteracted by the immensely large signature sizes of over 16,000 bytes and comparatively low levels of post-quantum security levels.

For approximately the same levels of post-quantum security, Dilithium and FALCON yield similar public key sizes, albeit much larger than classical primitives as RSA and ECDSA. FALCON, however, yields significantly smaller private key and signature sizes than Dilithium.

Performance comparison While classical algorithms were strictly better in all size comparisons, quantum-secure alternatives can have competitive sign and verify performance. SPHINCS+ is the slowest algorithm and comes with much longer signature creation and verification times, up to 100x slower signature creation times than classical ECDSA.

Dilithium and FALCON both have similarly low verify operations, even outperforming ECDSA by a large margin. Additionally, Dilithium even outperforms both RSA and ECDSA for signature creating times. Falcons signature creation performance is significantly higher than Dilithium.

In summary, SPHINCS+ comes with the most drawbacks of both large signature sizes and slow sign operations but having very small key sizes. Dilithium and FALCON come with different strengths and weaknesses: Dilithium has a much better signature creation performance, while Falcon comes with smaller key and signature sizes. Hence, the choice of which algorithm to use strongly depends on the concrete size and requirements and must be tailored to each particular use case.

4 Cryptographic inventory

In this section, we will go into greater detail about the cryptographic mechanisms employed in a digital asset ecosystem, and how they can be made fit for post-quantum cryptography. The first point, public-key infrastructure, is only applicable to a CBDC, whereas the later points can also be applied to other types of (decentralized) digital assets.

4.1 Public-key infrastructure

In order to authenticate participating entities in the CBDC ecosystem, either to the central bank or to each other, employing certificates is a natural choice. Certificate owners can either be natural persons, such as customers of a commercial bank, or abstract entities such as a centrally managed service or a smart

card. Since the trust of customers to a CBDC is, as the name says, dependent on the customers' trust towards the central bank, it is also a natural choice to build a Public Key Infrastructure (PKI) managed by the central bank. Then, the trust in the authenticity of all entities in the CBDC ecosystem is derived from trusting one Root Certificate Authority (CA) certificate managed by the central bank. The central bank can exercise full control over which entities are eligible to partake in the ecosystem or, alternatively, delegate the trust by issuing sub CA certificates to trusted partners.

By verifying these certificates and their respective certificate chains, customers and services could always ensure that communication partners are trustworthy.

Since certificates usually have long validity periods, cryptographic agility must be carefully considered and planned, long before the threat by quantum computers materializes.

While there are different certificate formats, most prominently the X.509 format, the approaches to tackle quantum agility can be achieved similarly if the certificate offer extension fields or not (described in more detail below).

Transitioning to a quantum-secure PKI can be done abruptly, by deactivating the classical PKI and building a new PKI as soon as the quantum threat materializes. This approach, however, is in most cases not applicable nor desirable. Specifically, a CBDC ecosystem must ensure a constant run-time of the system without any interruptions.

A smooth transition to a quantum-secure PKI is both more desirable and more challenging. The transition must be initiated in time and would result in a transition period where both classical and quantum-secure algorithms are used in certificates simultaneously. These so-called hybrid certificates can be designed in two ways: composite and non-composite.

Composite certificates have been under consideration in an IETF draft [18] and describe how certificates with multiple signature algorithms could look like. There are two options being discussed: with and without extension fields.

In case the certificate format allows for extension fields, as for example X.509, then a quantum-secure signature algorithm would be included in a certificate in such an extension field [18, 19].

In case extension fields are not existing in the used certificate format, the classical and quantum-secure algorithm information would exist in the same field in the certificate; either by concatenation or by clear separation within the certificate field. In this case, certificates parsing would need to be adjusted in all relying parties.

In both cases, a transition can be made smoothly. Policy makers could enforce certificate verifications to entail either only the classical algorithm, or the quantum-secure algorithm, or both. This policy adjustment can be made in run-time, and would not require any interference by the central bank with any circulating certificates.

An inevitable disadvantage of composite certificates is the larger size of the certificates resulting from the additional key material and signatures. Particu-

larly bearer-tokens as smart cards could have difficulties with the resulting larger certificates. An informed choice of algorithm (see also Section 3.3) is necessary.

Alternatively, the idea of **non-composite certificates** is that instead of including all the key material in the same certificates, every entity in the PKI could also be equipped with two separately issued certificates. These certificates do not need to be issued at the same time, but can be issued at different points in time. The certificates must be, however, linked to each other by a reference mechanism [3].

The CSR for the certificate with the quantum-secure certificate would be signed with the private key corresponding to the classical certificate. This approach also results in greater flexibility, as the policy makers could also enforce verification requirements on the relying parties. Either only the classical-certificate, or only the quantum-secure certificate, or both verifications must be successful.

4.2 Algorithm choice in the CBDC ecosystem

We now discuss suitable algorithms for various types of key material.

PKI root keys The choice of quantum-secure algorithms in a PKI greatly depends on the requirements arising from which entities create, manage, and verifies the certificates. For example, a root CA key has highest security requirements and must be stored securely at the central bank in an air-gapped HSM. Regular signature operations are not expected and small private key material is also not necessary. These requirements can, therefore, be ignored. The public key and signature sizes are important, however, since all relying parties in the PKI must securely store the root CA certificate locally to be able to verify all certificate chains. In the case when hardware is used as a bearer instrument for CBDC, e.g. a smart card, hybrid certificates for a smooth post-quantum transition would come with large root CA certificate sizes.

FALCON would be a suitable choice for the root CA signature algorithm, since the slightly longer signature creation times are outweighed by the smaller signature sizes.

Account and wallet keys Account and/or wallet keys (depending on the CBDC model) are long-lived: the key material is created once and is persists for a long time, up to many years. They are most likely part of the centrally managed PKI to ensure that only authenticated accounts and wallets partake in the CBDC ecosystem. That said, the key usage might differ according to the design specifications of the payment protocols. Account and wallet keys can be used to establish a secure channel by means of classical ECDH or, for post-quantum security, CRYSTALS-Kyber, since it is the only selected PKE/KEM algorithm by NIST. A symmetric AES key is negotiated and derived by choosing the appropriate key derivation functions (KDFs) and hash lengths.

For maximum flexibility, it is also a viable option to choose different algorithms within the same PKI. For example, in the case that wallet certificates are used to sign CBDC transactions, the expected number of sign operations is very high in contrast to a root CA certificate. Furthermore, private key material of a root CA certificate does not have strict size and performance requirements since it is stored in an HSM, which are capable of handling large key sizes sufficiently fast. Conversely, private key material of wallet certificates could be stored in devices with limited memory.

Therefore, FALCON and Dilithium are viable algorithm choices for root CA certificates. For end certificates with a high expected number of sign operations, FALCON is the better choice. SPHINCS+ is not recommended for either because of the large signature sizes.

Token keys Tokens are keys that are created both at the central bank (minting process) but also in wallets during regular operations. In contrast to account and wallet keys, token keys are short-lived and are not part of any PKI. (See also Section 5.3 for a more detailed discussion of cipher upgrades for tokens.)

Since token keys are created and deleted regularly, a new arising requirement are short key pair generation times.

While Dilithium has much lower key pair generation times than FALCON or SPHINCS+ [15], Dilithium signatures are up to three times as large as FALCON signatures (see above). Therefore, the choice between FALCON or Dilithium for token key material strongly depends on the concrete design of the payment protocols and the expected number of key creations and limitations in memory for token signatures. As mentioned above, SPHINCS+ is not suited for token keys because of the large signature sizes.

Other long- and short-lived keys Apart from the key material discussed above, other keys and certificates might be used for digital assets. For example, the central bank register responsible to validate transactions is a crucial component for security. Transaction must be verified and a receipt must be returned to the payer or payee to trust and finish the transaction. These receipts require a trustworthy signature from the register. The certificate used for receipt signatures has a long validity period with low key size and key generation time requirements, but must perform an abundance of signatures to verify transactions. Since Dilithium has much faster signature creation times than FALCON and SPHINCS+, Dilithium is a good choice for a register certificate.

5 Rolling upgrades

The requirements for a production-grade, widely available CBDC, outlined in the introductions, imply that the system cannot be stopped for a coordinated upgrade of cryptographic algorithms. Therefore, any upgrade roadmap must consider a rolling upgrade strategy. Especially popular in operations of large-scale distributed systems, a rolling upgrade entails a step-by-step upgrade of

individual components with a specified timeframe in which old and new versions can coexist and continue to interact.

Key questions now include:

- How should a component be designed to enable both forward (old system understands new instructions) and backward (new system understand old instructions) compatibility?
- How long should the timeframe for compatibility be?
- Can the upgrade be coordinated effectively?

Despite the similarities between cryptocurrencies and CBDC that we have alluded to earlier, their answers to these key questions differ dramatically. Hence, we will focus this section on CBDC.

5.1 Design decisions that may influence upgrade strategy

An important dimension in CBDC design is the use of software- and hardware-based wallets for transactions. In more ambitious designs, hardware wallets can be used both in online and offline payment scenarios and exchange money with other hardware wallets, but also software wallets.

Software-based wallets can come in many shapes, e.g. as a smartphone app, but also as a database entry managed by a financial intermediary, such as a commercial bank. In the latter case, upgrades would be completely transparent to the user.

For hardware-based wallets, the form factor is a core consideration. The cheapest form factor available is a commodity smart card, like what is in use today with credit or debit cards. Using CBDC on smart cards relies on availability of hardware acceleration for cryptographic algorithms (such as ECDSA with particular curve parameters) to be feasible. Typically, implementors do not have the ability to choose from a variety of algorithms.

Another dimension to be considered is whether self-custody is allowed, a topic that is hotly debated in literature [8,9]. Simply speaking, a CBDC offering self-custody would enable individual users to provision their own wallets, based on hardware and software that they deem fit. Central banks, or financial intermediaries that act as wallet issuers, would have significantly reduced control over the evolution of such self-custody wallets. For that reason, we exclude them from further discussions.

5.2 Wallet identification

In cryptocurrencies, addresses are computed from private cryptographic material. For example, an Ethereum address is computed by hashing an elliptic curve public key. Wallets would scan the blockchain for any transaction involving this address. While this avoids the problem of routing payments to particular entities based on e.g. address prefixes, like in IBANs, the downside is that the address of the asset is conflated with the identity to the wallet.

This conflation can be dissolved in CBDCs, where wallet identifiers do not have to be coupled to the cryptographic keys stored therein. In fact, a wallet identifier could be akin to a traditional bank account number, which stays fixed over the lifetime of a bank account, even though internal implementations details may change. Similarly, a credit card number would stay the same even after the physical credit card is replaced.

The reason for this discrepancy is that in CBDC, which should be accessible to the broad public without in-depth knowledge of cryptography, it would be poor user experience to change wallet identifiers if the algorithm changes.

Therefore, we propose that wallet identifiers should not be based on private cryptographic material, but are randomized upon creation and remain stable over time (“agnostic identifiers”). Note that such identifiers are only used for routing in online payment scenarios, i.e., for a sending wallet to identify the entity managing the receiving wallet. Offline payment scenarios do not require routing due to physical proximity. But more importantly, the central bank register can be made oblivious to identifiers, since it only concerns itself with digital signatures from the key material associated with the assets themselves, therefore avoiding a privacy risk.

The disadvantage of this approach is that agnostic identifiers, as opposed to a Bitcoin or Ethereum address, cannot be used to deduce which cryptographic algorithm is supported. This is balanced by the advantage that agnostic identifiers can support multiple algorithms with full transparency.

The remainder of this section discusses token upgrade strategies in general, and hardware concerns based specifically on agnostic identifiers.

5.3 Token upgrade strategies

As mentioned earlier, rolling updates are already a routine process in backend systems. In the case of new cryptographic algorithms, forward compatibility is much more difficult to achieve than backward compatibility. As an example, consider adding a data field to a message: forward compatibility is satisfied if a component can ignore the new data field and can still process the message. But a new cryptographic algorithm would need to be available on the component, otherwise the message cannot be understood.

Instead, focus should be placed on careful backwards compatibility, coupled with feature detection, if necessary.

Consider a hypothetical upgrade of a cryptographic algorithm, e.g. replacing ECDSA with FALCON as digital signature scheme for CBDC tokens. ECDSA and FALCON have different private key formats and lengths, therefore necessitating a dedicated process.

As a first step, the central bank would equip its register with the new cryptographic algorithm. In the case of a token-based CBDC, the register would need to offer a way to convert old-style EC tokens to FALCON tokens. But since such a CBDC would already support a transaction where one EC token can be exchanged for another one, simply adding a “token version” field in the token

format easily enables this kind of protocol evolution. The case of hybrid schemes may complicate implementation details, but can still be achieved in this manner.

This new algorithm becomes available at a certain point in time, with the central bank mandating a deadline of migrating all tokens. For simplicity, we use “new wallet” and “old wallet” to refer to wallets held in software components that are or are not aware of FALCON yet. Recall that with agnostic wallet identifiers, the sending wallet would not be able to deduce the supported key formats of the receiving wallet.

Now, we distinguish between the following cases and subcases for transactions, and discuss a migration strategy for each:

1. old wallet paying to old wallet
 - (a) EC tokens: works unmodified
 - (b) FALCON tokens: would not occur
2. old wallet paying to new wallet
 - (a) EC tokens: new wallet needs to be backwards compatible, auto-detection possible
 - (b) FALCON tokens: would not occur
3. new wallet paying to old wallet
 - (a) EC tokens: works unmodified
 - (b) FALCON tokens: only works if register supports version downgrade
4. new wallet paying to new wallet
 - (a) EC tokens: new wallet needs to be backwards compatible, auto-detection possible
 - (b) FALCON tokens: works unmodified

Backwards-compatible auto-detection is trivial to implement, since the receiving wallet merely needs to check the version of the incoming token.

The opposite direction, namely detecting if a receiving wallet only supports an earlier version (case 3) can be solved by imitating HTTP-style content negotiation: when the sending wallet initiates a payment, it first contacts the receiving wallet and offers a set of token versions, which will then be selected by the receiving wallet.

Should a version downgrade (subcase 3b) not be desired or implemented by the central bank, it is advisable that wallet operators avoid premature conversion before the deadline for migration (subcases 2a and 4a). This should be weighed against the possibility to run small trials of a new cryptographic algorithm to gather more experience, and slowly ramp up the percentage of wallets that use the new version.

Note that this upgrade strategy can also be applied for other protocol changes, e.g. increasing the resolution of monetary values (two decimal digits to four decimal digits).

5.4 Hardware upgrade strategies

While token upgrades in hardware wallets follow the same logic as described in the previous section, there are some additional considerations relating to their restricted compute power and their offline capability.

Typical credit or debit cards have expiration times between three to five years. Therefore, consumers are already familiar with the procedure of routinely exchanging payment cards. Since simple smart cards are easy to manufacture and distribute, we anticipate no significant issues leveraging this strategy to upgrade CBDC hardware wallets.

A problem remains if a CBDC is offline-capable. Some implementations use deferred communication between hardware wallets and the central bank register: transactions instantly settle even offline, but wallets keep a record of digital signatures to upload them to the register and have them validated at a later point. This may complicate subcase 3b, which should be avoided in such a setting.

Applied to the above example, this would imply the following timeline:

- At a particular time, FALCON becomes available at the register.
- Soon afterwards, hardware wallets supporting both EC and FALCON become available. They never upgrade tokens unless prompted by receiving a FALCON token.
- Once all users have obtained new wallets (to be defined as a soft deadline), all software wallets upgrade tokens. FALCON tokens start to appear in hardware wallets, due to software-to-hardware top-ups.
- Slowly, the hardware wallet ecosystem upgrades, due to hardware-to-hardware payments.

The hard migration deadline, i.e. the time when the register would no longer accept EC tokens, would need to be defined to be at least the soft deadline, plus validity of the new hardware wallets. An additional safety margin would allow users to exchange their funds in case they let a wallet sit unused for an extended amount of time, similarly to how the Eurozone’s national banks to this date still allow exchange of local currency to the Euro.

Perfect enforcement of the aforementioned deadlines is almost impossible in any manner, since hardware wallets in full offline operation may not have access to trusted clocks [6].

Finally, we will briefly consider point-of-sale (or other payment) terminals. In the case of online terminals, support for new algorithms can be added through routine over-the-air updates. For pure offline terminals, this is naturally not possible.

Therefore, it is advantageous to design the payment protocol between hardware wallets to be independent of the communication channel and the terminal. Concretely, the terminal and wallet(s) may have a shared interface for payment lifecycle (initiation, retry, cancelation), but the token-level protocol is opaque towards the terminal. This prevents the need for terminal upgrades altogether. On a low level, this can be achieved by modularizing terminals and allowing merchants to merely exchange the smart card (or chip) on which the wallet resides.

6 Conclusion

We have discussed how the advent of quantum computing affects the kind of cryptography used in digital assets, more specifically, a central bank digital currency (CBDC). In particular, the problem that elliptic curve private keys could be computed by quantum attackers merely by the disclosure of the corresponding public key is a looming issue that threatens safe custody of assets. Even worse, it could lead to loss of funds without any user interactions whatsoever.

While many concerns are shared between CBDC and cryptocurrency, the universal nature of CBDC poses additional challenges: for example, upgrades of cryptographic algorithms must be completely transparent to users as to not hinder adoption. However, given that CBDC is also more centralized, it stands to reason that central banks can use their more granular control over the ecosystem to ensure smooth transitions.

We have shown that a digital asset ecosystem comes with a great deal of key material with a multitude of different requirements. The choice of the correct quantum-secure algorithm in accordance with NIST recommendations is, therefore, not straightforward and must be considered carefully. In order to grant full flexibility for crypto agility, we proposed not choosing one algorithm for all components, but instead select the algorithm for each specific component.

Our proposed cryptographic upgrade framework enables just that and can be applied to a token-based CBDC design. The framework’s cornerstones are the use of agnostic wallet identifiers, decoupling user-facing addresses from private key material, and a conservative upgrade strategy relying on auto-detection of wallet capabilities. We expect this framework to be used for both software and hardware wallets, and potentially for self-custodial wallets as well.

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